

COBIZ INC
Form 10-Q
November 09, 2006

U.S. 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 September 30, 2006.

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transitions period from _____ to _____

Commission File Number 001-15955

CoBiz Inc.

(Exact name of registrant as specified in its charter)

COLORADO
(State or other jurisdiction of
incorporation or organization)

84-0826324
(I.R.S. Employer
Identification No.)

821 17th Street
Denver, CO
(Address of principal executive offices)

80202
(Zip Code)

(303) 293-2265
(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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer (see definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act).

Large Accelerated Filer Accelerated Filer Non-accelerated Filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

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There were 22,671,047 shares of the registrant's Common Stock, \$0.01 par value per share, outstanding as of November 2, 2006.

PART I. FINANCIAL INFORMATION

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Item 1. Financial Statements

CoBiz Inc

Consolidated Balance Sheets

September 30, 2006 and December 31, 2005

(unaudited)

	September 30, 2006	December 31, 2005
	(dollars in thousands)	
Assets		
Cash and due from banks	\$ 58,789	\$ 50,701
Investments:		
Investment securities available for sale (cost of \$459,232 and \$459,952, respectively)	453,797	453,296
Investment securities held to maturity (fair value of \$766 and \$902, respectively)	763	893
Other investments	15,297	11,961
Total investments	469,857	466,150
Loans, net	1,498,779	1,315,762
Goodwill	38,961	38,446
Intangible assets, net	2,701	3,058
Bank owned life insurance	25,347	24,578
Premises and equipment, net	8,445	9,219
Accrued interest receivable	7,667	7,261
Deferred income taxes	8,878	8,391
Other	11,044	9,490
TOTAL ASSETS	\$ 2,130,468	\$ 1,933,056
Liabilities		
Deposits		
Demand	437,571	436,091
NOW and money market	500,262	502,283
Savings	11,304	8,461
Certificates of deposits	447,200	380,117
Total Deposits	1,396,337	1,326,952
Securities sold under agreements to repurchase	246,346	216,726
Other short-term borrowings	241,373	165,000
Accrued interest and other liabilities	18,618	15,668
Junior subordinated debentures	72,166	72,166
TOTAL LIABILITIES	\$ 1,974,840	\$ 1,796,512
Shareholders Equity		
Cumulative preferred, \$.01 par value; 2,000,000 shares authorized; None outstanding		
Common, \$.01 par value; 50,000,000 shares authorized; 22,649,996 and 22,309,136 issued and outstanding, respectively	226	223
Additional paid-in capital	73,719	69,560
Retained earnings	86,377	72,636
Accumulated other comprehensive (loss) net of income tax of \$(2,876) and \$(3,599), respectively	(4,694)	(5,875)
TOTAL SHAREHOLDERS EQUITY	\$ 155,628	\$ 136,544
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	\$ 2,130,468	\$ 1,933,056

See Notes to Consolidated Financial Statements

CoBiz Inc.

Consolidated Statements of Income and Comprehensive Income

(unaudited)

	Three months ended September 30,		Nine Months ended September 30,	
	2006	2005	2006	2005
	(dollars in thousands)			
INTEREST INCOME:				
Interest and fees on loans	\$ 30,079	\$ 22,384	\$ 83,515	\$ 61,011
Interest and dividends on investment securities:				
Taxable securities	5,305	4,403	15,164	13,009
Nontaxable securities	56	60	173	172
Dividends on securities	199	116	550	345
Federal funds sold and other	120	48	297	166
Total interest income	35,759	27,011	99,699	74,703
INTEREST EXPENSE:				
Interest on deposits	9,023	5,134	23,640	12,392
Interest on short-term borrowings	5,134	2,582	13,452	6,840
Interest on junior subordinated debentures	1,438	996	4,022	3,219
Total interest expense	15,595	8,712	41,114	22,451
NET INTEREST INCOME BEFORE PROVISION FOR LOAN AND CREDIT LOSSES				
Provision for loan and credit losses	20,164	18,299	58,585	52,252
Provision for loan and credit losses	75	847	1,162	1,942
NET INTEREST INCOME AFTER PROVISION FOR LOAN AND CREDIT LOSSES				
	20,089	17,452	57,423	50,310
NONINTEREST INCOME:				
Service charges	679	678	2,104	2,150
Trust and advisory fees	1,030	978	3,054	2,947
Insurance income	3,525	2,389	9,088	7,721
Investment banking income	1,063	727	4,118	2,696
Other income	986	658	2,478	1,950
Total noninterest income	7,283	5,430	20,842	17,464
NONINTEREST EXPENSE:				
Salaries and employee benefits	11,855	9,795	34,219	29,141
Occupancy expenses, premises and equipment	2,961	2,814	8,517	8,181
Amortization of intangibles	118	137	357	416
Other	2,506	2,484	7,740	7,679
Loss on sale of other assets and securities	47	13	73	139
Total noninterest expense	17,487	15,243	50,906	45,556
INCOME BEFORE INCOME TAXES	9,885	7,639	27,359	22,218
Provision for income taxes	3,629	2,595	10,018	7,942
NET INCOME	\$ 6,256	\$ 5,044	\$ 17,341	\$ 14,276
UNREALIZED APPRECIATION (DEPRECIATION) ON INVESTMENT SECURITIES AVAILABLE FOR SALE AND DERIVATIVE INSTRUMENTS , net of tax				
	4,098	(1,550)	1,181	(3,199)
COMPREHENSIVE INCOME	\$ 10,354	\$ 3,494	\$ 18,522	\$ 11,077
EARNINGS PER SHARE:				
Basic	\$ 0.28	\$ 0.23	\$ 0.77	\$ 0.64

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Diluted	\$ 0.27	\$ 0.22	\$ 0.74	\$ 0.62
DIVIDENDS PER SHARE	\$ 0.06	\$ 0.05	\$ 0.16	\$ 0.14

CoBiz Inc.

Consolidated Statements of Cash Flows

For the Nine Months Ended September 30, 2006 and 2005

(unaudited)

	2006	2005
	(dollars in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 17,341	\$ 14,276
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,015	2,837
Write-down of impaired investment security		108
Provision for loan and credit losses	1,162	1,942
Federal Home Loan Bank stock dividend	(260)	(222)
Deferred income taxes	(884)	(769)
Increase in cash surrender value of bank owned life insurance	(769)	(761)
Stock-based compensation	855	
Excess tax benefits from stock-based compensation	(712)	
Other	461	261
Changes in operating assets and liabilities		
Accrued interest receivable	(419)	(1,062)
Other assets	(388)	(420)
Accrued interest and other liabilities	1,281	376
Net cash provided by operating activities	19,683	16,566
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of other investments	(4,762)	(2,457)
Repayment of other investments	630	
Purchase of investment securities available for sale	(93,190)	(105,251)
Maturities of investment securities held to maturity	130	267
Maturities of investment securities available for sale	92,692	120,991
Cash paid for earn-outs	(206)	(2,033)
Purchase of bank owned life insurance		(8,020)
Loan originations and repayments, net	(181,439)	(154,502)
Purchase of premises and equipment	(1,933)	(2,517)
Other	64	37
Net cash used in investing activities	(188,014)	(153,485)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in demand, NOW, money market, and savings accounts	3,945	84,106
Net increase in certificates of deposits	67,083	81,342
Net increase (decrease) in federal funds purchased	16,400	(9,650)
Net increase (decrease) in securities sold under agreements to repurchase	29,620	(37,338)
Advances from the Federal Home Loan Bank	3,950,570	2,100,350
Repayments of advances from the Federal Home Loan Bank	(3,890,597)	(2,065,350)
Issuance of junior subordinated debentures		20,000
Redemption of junior subordinated debentures		(20,000)
Proceeds from exercise of stock options	2,286	1,018
Dividends paid on common stock	(3,600)	(3,100)
Other	712	(75)
Net cash provided by financing activities	176,419	151,303
NET INCREASE IN CASH AND CASH EQUIVALENTS	8,088	14,384
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	50,701	32,345
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 58,789	\$ 46,729

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See notes to consolidated financial statements

CoBiz Inc. and Subsidiaries

Notes to Consolidated Condensed Financial Statements

(unaudited)

The accompanying unaudited consolidated condensed financial statements of CoBiz Inc. (Parent), and its wholly owned subsidiaries: CoBiz ACMG, Inc.; CoBiz Bank, N.A. (Bank); CoBiz Insurance, Inc.; Colorado Business Leasing, Inc. (Leasing); CoBiz GMB, Inc.; GMB Equity Partners; and Financial Designs Ltd. (FDL), all collectively referred to as the Company or CoBiz, conform to accounting principles generally accepted in the United States of America for interim financial information and prevailing practices within the banking industry. The Bank operates in its Colorado market areas under the name Colorado Business Bank (CBB) and in its Arizona market areas under the name Arizona Business Bank (ABB).

The Bank is a full-service business bank with eleven Colorado locations, including eight in the Denver metropolitan area, two locations in Boulder and one in Edwards, just west of Vail, as well as seven Arizona locations, all of which are in the Phoenix metropolitan area. CoBiz ACMG, Inc. provides investment management services to institutions and individuals through its subsidiary Alexander Capital Management Group, LLC (ACMG). FDL provides wealth transfer, employee benefits consulting, insurance brokerage and related administrative support to employers. CoBiz Insurance, Inc. provides commercial and personal property and casualty insurance brokerage, as well as risk management consulting services to small and medium-sized businesses and individuals. CoBiz GMB, Inc. provides investment banking services to middle-market companies through its wholly owned subsidiary, Green Manning and Bunch, Ltd. (GMB).

All significant intercompany accounts and transactions have been eliminated. These financial statements and notes thereto should be read in conjunction with, and are qualified in their entirety by, our Annual Report on Form 10-K for the year ended December 31, 2005, as filed with the Securities and Exchange Commission (SEC).

The consolidated condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting only of normally recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for the full year ending December 31, 2006. Certain reclassifications have been made to prior balances to conform to the current year presentation.

1. Earn-out Arrangements

General Earn-out payments for the ACMG and FDL transactions are treated as additional costs of the acquisitions and recorded as goodwill in accordance with EITF 95-08 *Accounting for Contingent Consideration Paid to the Shareholders of an Acquired Enterprise in a Purchase Business Combination*. Goodwill arising from these transactions is allocated between the operating segments expected to benefit from the acquisitions. See Note 5 **Goodwill and Intangible Assets** for the amount of goodwill allocated to each operating segment.

Alexander Capital Management Group LLC On April 1, 2003, the Company acquired ACMG, an SEC-registered investment advisory firm based in Denver, Colorado. The acquisition was accounted for

using the purchase method of accounting, and accordingly, the results of ACMG's operations have been included in the consolidated financial statements since the date of purchase. The acquisition of ACMG was completed through a merger of Alexander Capital Management Group, Inc. into a wholly owned subsidiary that was formed in order to consummate the transaction and then a subsequent contribution of the assets and liabilities of the merged entity into a newly formed limited liability company called Alexander Capital Management Group, LLC.

The aggregate purchase price was \$3,131,000, consisting of 160,830 shares of CoBiz Inc. common stock valued at \$1,500,000; \$1,277,000 in cash; \$264,000 in net liabilities assumed; and \$90,000 in direct acquisition costs (consisting primarily of external legal fees). Goodwill of \$2,916,000, which is not expected to be deductible for tax purposes, was recorded as part of the purchase price allocation. Intangible assets consisting of customer account relationships, employment agreements and non-solicitation agreements totaling \$346,000 were also recorded with an average useful life of 14 years.

The terms of the ACMG merger agreement provided for additional earn-out payments for each of the twelve months ended on March 31, 2004, 2005, and 2006 to be paid to the former shareholders of Alexander Capital Management Group, Inc. in proportion to their respective ownership immediately prior to the acquisition. All earn-out payments were made 40% in cash and 60% in CoBiz Inc. common stock.

The earn-out payment for the 12 months ended March 31, 2004 was equal to a multiple of ACMG's earnings before interest, taxes, depreciation, and amortization as defined in the ACMG merger agreement (ACMG EBITDA). The earn-out payments for 2005 and 2006 were equal to a multiple of the excess of each year's ACMG EBITDA over the ACMG EBITDA for the previous year. During 2004, the Company paid \$815,000 for the earn-out period ended on March 31, 2004 based on ACMG EBITDA of \$163,000. The payment consisted of \$326,000 in cash and 36,988 shares of CoBiz stock valued at \$489,000. During 2005 the Company paid \$2,243,000 for the earn-out period ended on March 31, 2005, based on ACMG EBITDA of \$611,000. The payment consisted of \$897,000 in cash and 68,215 shares of CoBiz Inc. stock valued at \$1,345,000. For the earn-out period ending March 31, 2006, the Company paid \$515,000 based on ACMG EBITDA of \$715,000. The payment consisted of \$206,000 in cash and 15,576 shares of CoBiz Inc. stock valued at \$309,000.

In addition to the earn-out, the former shareholders of Alexander Capital Management Group, Inc. were issued 200,000 Profits Interest Units pursuant to the Operating Agreement of ACMG, representing a 20% interest in the profits and losses of ACMG in periods following the acquisition (but no interest in the value of ACMG as of the date of the acquisition), which is reflected in the accompanying consolidated statements of condition as a component of Accrued interest and other liabilities and is included in Other noninterest expense in the consolidated statements of income and comprehensive income. Unlike the earn-out payments, which are based on a multiple of earnings for a specified period of time, the Profits Interest Units entitle the holders to share in the earnings of ACMG for as long as they are held. Pursuant to the terms of a Unitholders Agreement executed by all former shareholders of Alexander Capital Management Group, Inc., under certain circumstances, the Company has the ability to call the Profits Interest Units at a price based on a multiple of the trailing 12 months ACMG EBITDA. Likewise, the holders of the Profits Interest Units have, under certain circumstances, the ability to put the Profits Interest Units to the Company at a price based on a multiple of the trailing 12 months ACMG EBITDA.

Financial Designs Ltd. On April 14, 2003, the Company acquired FDL, a provider of wealth transfer and employee benefit services based in Denver, Colorado. The acquisition was accounted for using the purchase method of accounting, and accordingly, the results of FDL's operations have been included in

the consolidated financial statements since the date of purchase. The acquisition of FDL was completed through a merger of FDL into CoBiz Connect, Inc., a wholly owned subsidiary of CoBiz that had provided employee benefits consulting services since 2000. The surviving corporation continues to use the FDL name.

The aggregate purchase price was \$5,406,000, consisting of 333,472 shares of CoBiz Inc. common stock valued at \$3,210,000; \$2,140,000 in cash; and \$56,000 in direct acquisition costs (consisting primarily of external legal fees). Goodwill of \$3,097,000, which is not expected to be deductible for tax purposes, was recorded as part of the purchase price allocation. Intangible assets consisting of customer account relationships, employment agreements and non-solicitation agreements totaling \$3,045,000 were also recorded with an average useful life of 10 years.

The terms of the FDL merger agreement provide for additional earn-out payments for each of the calendar years 2003 through 2007 to be paid to the former shareholders of FDL in proportion to their respective ownership immediately prior to the acquisition. The earn-out payments are payable 50% in cash and 50% in CoBiz Inc. common stock.

The earn-out payment for the 2003 calendar year was equal to a multiple of FDL's earnings before interest, taxes, depreciation, and amortization as defined in the FDL merger agreement (FDL EBITDA) for 2003. During 2004, the Company paid \$18,898,000 for the 2003 earn-out payment owed to the former shareholders of FDL based on FDL EBITDA of \$3,485,000 for 2003, which had previously been accrued in 2003. The payment consisted of \$9,449,000 in cash and 813,948 shares of CoBiz Inc. common stock valued at \$9,449,000. No earn-out payments were payable for the 2004 and 2005 calendar years.

The earn-out payments for the 2006 and 2007 calendar years will be calculated on the excess of each calendar year's FDL EBITDA over a hurdle rate which is equal to the highest previously recognized FDL EBITDA for the 2004 through 2006 calendar years. The earn-out payments for these calendar years will be based on a range of multiples, dependent on performance.

The merger agreement does not provide for a minimum earn-out, nor does it cap the total amount that may be paid. Therefore, future earn-outs payments will depend on the financial results of FDL during the earn-out period. Management estimates that total cumulative earn-out payments for 2006 and 2007 may range from \$0 to \$600,000.

2. Recent Accounting Pronouncements

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 123(R), *Share-Based Payment* (SFAS 123(R)) using the modified prospective method. Under this method, compensation cost is recognized for (1) all awards granted after the required effective date and to awards modified, cancelled, or repurchased after that date and (2) the portion of prior awards for which the requisite service has not yet been rendered, based on the grant-date fair value of those awards calculated for pro forma disclosures under SFAS 123, *Accounting for Stock Based Compensation*. Prior to the adoption of SFAS 123(R), the Company applied the intrinsic-value method for its stock-based compensation plans in accordance with Accounting Principles Board Opinion No. 25 (APB 25) *Accounting for Stock Issued to Employees*, which was allowed by SFAS 123 as an alternative to the fair value method recommended by SFAS 123.

SFAS 123(R) requires that the cash retained as a result of the tax deductibility of employee share-based awards be presented as a component of cash flows from financing activities in the consolidated

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statement of cash flows. In prior periods, this amount was reported as a component of cash flows from operating activities. The adoption of SFAS 123(R) had the following impact on our consolidated financial statements for the nine months ending September 30, 2006:

(dollars in thousands, except per share amounts)	Increase/(Decrease)
Income before income taxes	\$ (855)
Net income	(709)
Earnings per share - basic	(0.03)
Earnings per share - diluted	(0.03)
Cash used by operating activities	(712)
Cash provided by financing activities (tax benefit)	712

SFAS 123(R) specifies that the fair value of an employee stock option must be based on an observable market price of an option with the same or similar terms and conditions if one is available or, if an observable market price is not available, the fair value must be estimated using a valuation technique that (1) is applied in a manner consistent with the fair value measurement objective and the other requirements of the Statement, (2) is based on established principles of financial economic theory and generally applied to that field, and (3) reflects all substantive characteristics of the instrument. SFAS 123(R) permits entities to use any option-pricing model that meets the fair value objective in the Statement.

On January 1, 2006, the Company adopted SFAS No. 154, *Accounting Changes and Error Corrections Disclosure* (SFAS 154). SFAS 154 replaces APB Opinion No. 20, *Accounting Changes* and SFAS No. 3, *Reporting Accounting Changes in Interim Financial Statements*. SFAS 154 requires retrospective application to prior periods financial statements of changes in accounting principle unless it is impracticable. SFAS 154 applies to all voluntary changes in accounting principle. It also applies to changes required by a new accounting pronouncement in the unusual instance that the pronouncement does not include explicit transition provisions. For example, the retrospective provision of SFAS 154 does not apply to the adoption of SFAS 123(R) which includes specific transition provisions. The adoption of SFAS 154 did not have a material impact on our consolidated financial statements.

On January 1, 2006 the Company adopted EITF Issue No. 04-05, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights* (EITF 04-05). The scope of EITF 04-05 is limited to limited partnerships or similar entities that are not variable interest entities under FIN 46. The EITF reached a consensus that the general partners in a limited partnership (or similar entity) are presumed to control the entity regardless of the level of their ownership and, accordingly, may be required to consolidate the entity. This is a rebuttable presumption that may be overcome if the partnership agreements provide the limited partners with either (a) the substantive ability to dissolve (liquidate) the limited partnership or otherwise remove the general partners without cause or (b) substantive participating rights. If it is deemed that the limited partners rights overcome the presumption of control by a general partner of the limited partnership, the general partner shall account for its investment in the limited partnership using the equity method of accounting. EITF 04-05 became effective immediately for all arrangements created or modified after June 29, 2005. For all other arrangements, application of EITF 04-05 became effective for the first reporting period in fiscal years beginning after December 15, 2005. The adoption of EITF 04-05 did not have a material impact on our consolidated financial statements.

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes- an Interpretation of SFAS No. 109* (FIN 48). FIN 48

prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact FIN 48 will have on its consolidated financial statements.

In September 2006, the Emerging Issues Task Force (EITF) reached a consensus on EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements* (EITF 06-4). The consensus, which has been ratified by the Financial Accounting Standards Board, requires companies to recognize an obligation for the future post-retirement benefits provided to employees in the form of death benefits to be paid to their beneficiaries through split-dollar policies carried in Bank Owned Life Insurance (BOLI). EITF 06-4 is effective for fiscal periods beginning after December 15, 2007. The effects of applying EITF 06-4 are to be recognized through either (a) a change in accounting principle through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption, or (b) a change in accounting principle through retrospective application to all prior periods. The Company is currently evaluating the impact EITF 04-6 will have on its consolidated financial statements, as the Company has issued endorsement split-dollar life-insurance arrangements.

3. Earnings per Common Share

The weighted average shares outstanding used in the calculation of basic and diluted earnings per share are as follows:

	Three months ended September 30, 2006		Nine months ended September 30, 2006	
	2005	2005	2005	2005
Weighted average shares outstanding - basic earnings per share	22,612,232	22,216,672	22,503,528	22,135,110
Effect of dilutive securities	824,875	878,408	818,095	946,370
Weighted average shares outstanding - diluted earnings per share	23,437,107	23,095,080	23,321,623	23,081,480

For the three and nine months ended September 30, 2006, 335,496 and 366,119 options, respectively, were excluded from the earnings per share computation solely because their effect was anti-dilutive. For the three and nine months ended September 30, 2005, 244,168 and 138,399 options, respectively, were excluded from the earnings per share computation solely because their effect was anti-dilutive.

4. Comprehensive Income

Comprehensive income is the total of (1) net income plus (2) all other changes in net assets arising from non-owner sources, which are referred to as other comprehensive income. Presented below are the changes in other comprehensive income for the periods indicated.

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	Three months ended September 30, 2006 (in thousands)		Nine Months ended September 30, 2006 2005	
Other comprehensive items:				
Unrealized gain (loss) on available for sale securities arising during the period	\$ 5,372	\$ (1,104)	\$ 1,173	\$ (2,857)
Unrealized gain (loss) on derivative securities arising during the period	1,191	(1,383)	683	(2,282)
Reclassification adjustment for realized (gains) losses arising during the period	47	(13)	48	(19)
Tax benefit (expense) related to items of other comprehensive income	(2,512)	950	(723)	1,959
Other comprehensive income (loss), net of tax	\$ 4,098	\$ (1,550)	\$ 1,181	\$ (3,199)

5. Goodwill and Intangible Assets

A summary of goodwill, adjustments to goodwill and total assets by operating segment as of September 30, 2006, is noted below. The increase in goodwill is primarily related to the ACMG 2006 earn-out which was paid in the second quarter of 2006.

	Goodwill December 31, 2005 (dollars in thousands)	Acquisitions and adjustments	September 30, 2006	Total assets September 30, 2006
Colorado Business Bank	\$ 13,035	\$ 155	\$ 13,190	\$ 1,445,799
Arizona Business Bank	1,704	26	1,730	645,970
Investment banking services	5,279		5,279	8,170
Investment advisory and trust	3,883	334	4,217	5,988
Insurance	14,545		14,545	21,822
Corporate support and other				2,719
Total	\$ 38,446	\$ 515	\$ 38,961	\$ 2,130,468

As of December 31, 2005, and September 30, 2006, the Company's intangible assets and related accumulated amortization consisted of the following:

	Customer contracts, lists and relationships (dollars in thousands)	Employment and non-solicitation agreements	Total
December 31, 2005	\$ 3,014	\$ 44	\$ 3,058
Amortization	344	13	357
September 30, 2006	\$ 2,670	\$ 31	\$ 2,701

The Company recorded amortization expense of \$357,000 during the nine months ended September 30, 2006, compared to \$416,000 in the same period of 2005. Amortization expense on intangible assets for each of the five succeeding years is estimated as follows (dollars in thousands):

2007	\$ 472
2008	413
2009	364
2010	363
2011	360
Total	\$ 1,972

6. Derivatives

A summary of the outstanding derivatives at September 30, 2006 is as follows:

	September 30, 2006		2005	
	Notional (dollars in thousands)	Estimated fair value	Notional	Estimated fair value
Asset/liability management hedges:				
Cash flow hedges - interest rate swap	\$ 130,000	\$ (2,136)	\$ 165,000	\$ (2,517)
Customer accomodation derivatives:				
Interest rate swaps	\$ 13,205	\$ (305)	\$ 1,078	\$ 30
Reverse interest rate swaps	13,205	305	1,078	(30)

7. Junior Subordinated Debentures

A summary of the outstanding junior subordinated debentures at September 30, 2006 is as follows:

	Interest Rate	Junior Subordinated Debentures	Maturity Date	Earliest Call Date
CoBiz Statutory Trust I	3-month LIBOR + 2.95 %	\$ 20,619,000	September 17, 2033	September 17, 2008
CoBiz Capital Trust II	3-month LIBOR + 2.60 %	\$ 30,928,000	July 23, 2034	July 23, 2009
CoBiz Capital Trust III	3-month LIBOR + 1.45 %	\$ 20,619,000	September 30, 2035	September 30, 2010

8. Share-Based Compensation Plans

The Company has adopted several stock option plans (Plans) to reward and provide long-term incentives for directors and key employees of the Company. Options issued from the Plans have terms between seven and ten years. Options are typically issued with vesting periods ranging from immediate vesting to three-to-four year graded vesting schedules. The Company's policy is to issue new shares upon the exercise of an option.

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The 1997 Incentive Stock Option Plan (the 1997 Plan) authorizes the issuance of 227,331 shares at not less than the market value of the Company's stock at the date of grant. The majority of the options issued under the 1997 Plan are exercisable commencing one year from the date of grant and vest 25% per year thereafter becoming fully exercisable after four years. Shares available for grant as of September 30, 2006 totaled 2,164.

The 1998 Stock Incentive Plan (the 1998 Plan) authorizes the issuance of 956,250 shares of Common Stock. The exercise price for options granted under the 1998 Plan must be at least equal to 100% of the fair market value of the Common Stock on the date of grant. The 1998 Plan permits the granting of incentive Stock Options and non-qualified stock options. Options granted under the 1998 Plan have vesting schedules ranging from immediately exercisable to being exercisable four years from the date of grant. Shares available for grant as of September 30, 2006 totaled 633.

The 2002 Equity Incentive Plan (the 2002 Plan) authorizes the issuance of 975,000 shares of Common Stock. Under the 2002 Plan, the Compensation Committee of the Company has the authority to determine the identity of the key employees, consultants, and directors who shall be granted options; the option price, which shall not be less than 85% of the fair market value of the Common Stock on the date of grant; and the manner and times at which the options shall be exercisable. Shares available for grant as of September 30, 2006 totaled 47,855.

The 2005 Equity Incentive Plan (the 2005 Plan) authorizes the issuance of 1,250,000 shares of Common Stock. Under the 2005 Plan, the Compensation Committee of the Company has the authority to determine the identity of the key employees, consultants, and directors who shall be granted options; the option price, which shall not be less than 85% of the fair market value of the Common Stock on the date of grant; and the manner and times at which the options shall be exercisable. Shares available for grant as of September 30, 2006 totaled 693,732.

During the first nine months of 2006, the Company recognized compensation expense, net of estimated forfeitures, of \$855,000 for stock-based compensation awards for which the requisite service was rendered in the first nine months of 2006.

The following table illustrates the effect on net income and income per share if the fair value based method had been applied to all outstanding and unvested awards for the three and nine months ended September 30, 2005:

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	Three months ended September 30, 2005 (dollars in thousands)	Nine months ended September 30, 2005
Net income, as reported	\$ 5,044	\$ 14,276
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects		
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(227)	(709)
Pro forma net income	\$ 4,817	\$ 13,567
Earnings per share:		
As reported - basic	\$ 0.23	\$ 0.64
As reported - diluted	\$ 0.22	\$ 0.62
Pro forma - basic	\$ 0.22	\$ 0.61
Pro forma - diluted	\$ 0.21	\$ 0.59

SFAS 123(R) requires the Company to select a valuation technique that meets the measurement criteria set forth in the Standard. Valuation techniques that meet the criteria for estimating the fair values of employee stock options include a lattice model and a closed-form model (for example, the Black-Scholes formula). The Company is currently using the Black-Scholes model to estimate the fair value of stock options.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model (the Model). The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield in effect at the time of grant. The expected term of options granted is based on the options vesting schedule and the Company's historical exercise patterns and represents the period of time that options granted are expected to be outstanding. Expected volatilities are based on the historical volatility of the Company's stock and vesting period of the option to be issued. The dividend yield is determined by annualizing the dividend rate at the time of grant as a percentage of the Company stock price at the time of grant. The following weighted average assumptions were used for grants issued in the three and nine months ending September 30, 2006 and 2005:

	Three months ended September 30,		Nine months ended September 30,	
	2006	2005	2006	2005
Risk-free interest rate	4.78 %	4.00 %	4.92 %	3.74 %
Expected life in years	3.5	3.5	3.5	4.0
Volatility	30.27 %	24.83 %	30.93 %	25.58 %
Expected dividend yield	0.94 %	1.04 %	1.01 %	0.98 %

The range of risk-free interest rates used in the model during the three months ending September 30, 2006 was 4.66% to 5.12%. The range of expected volatility used in the model was 29.01% to 32.47%. The range of expected dividend yields used in the model was 0.85% to 0.97%. The range of risk-free interest rates used in the model during the nine months ending September 30, 2006 was 4.49% to 5.12%. The range of expected volatility used in the model was 29.01% to 33.88%. The range of expected dividend yields used in the model was 0.85% to 1.09%.

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The range of risk-free interest rates used in the model during the three months ending September 30, 2005 was 3.83% to 4.09%. The range of expected volatility used in the model was 23.44% to 25.75%. The range of expected dividend yields used in the model was 1.03% to 1.05%. The range of risk-free interest rates used in the model during the nine months ending September 30, 2005 was 3.31% to 4.33%. The range of expected volatility used in the model was 23.23% to 28.08%. The range of expected dividend yields used in the model was 0.87% to 1.05%.

The summary of changes in shares under option for the nine months ended September 30, 2006 is as follows:

	Shares	Weighted average exercise price
Outstanding, beginning of year	2,203,184	\$ 10.54
Granted	326,001	21.39
Exercised	(298,200)	5.81
Forfeited	(45,157)	16.15
Outstanding, end of period	2,185,828	\$ 12.69
Options exercisable, end of period	1,518,324	\$ 9.99

The weighted average remaining terms for options outstanding and options exercisable at the end of the period was 5.5 and 4.9 years, respectively. The aggregate intrinsic value for options outstanding and options exercisable at the end of the period was \$22,240,000 and \$19,547,000, respectively. The weighted-average grant-date fair value of options granted during the nine months ended September 30, 2006 was \$4.92. The total intrinsic value of options exercised during the nine months ended September 30, 2006 was \$4,356,000.

As of September 30, 2006, there was \$2,357,000 of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the Plans. The cost is expected to be recognized over a weighted average period of 2.3 years.

10. Segments

The Company's principal areas of activity consist of commercial banking, investment banking, investment advisory and trust, insurance, and corporate support and other.

The Company distinguishes its commercial banking segments based on geographic markets served. Currently, reportable commercial banking segments are CBB and ABB. CBB is a full-service business bank with eleven Colorado locations, including eight in the Denver metropolitan area, two locations in Boulder and one in Edwards, just west of Vail. ABB is based in Phoenix, Arizona and has seven locations in the Phoenix metropolitan area.

The investment banking services segment consists of the operations of GMB, which provides middle-market companies with merger and acquisition advisory services, institutional private placements of debt and equity, and other strategic financial advisory services.

The investment advisory and trust segment consists of the operations of ACMG and CoBiz Private Asset Management (PAM). ACMG is an SEC-registered investment management firm that manages stock and bond portfolios for individuals and institutions. CoBiz Private Asset Management offers wealth management and investment advisory services, fiduciary (trust) services, and estate administration services.

The insurance segment includes the activities of FDL and CoBiz Insurance, Inc. FDL provides employee benefits consulting and brokerage, wealth transfer planning and preservation for high-net-worth individuals, and executive benefits and compensation planning. FDL represents individuals and companies in the acquisition of institutionally priced life insurance products to meet wealth transfer and business needs. Employee benefit services include assisting companies in creating and managing benefit programs such as medical, dental, vision, 401(k), disability, life and cafeteria plans. CoBiz Insurance, Inc. provides commercial and personal property and casualty insurance brokerage, as well as risk management consulting services to individuals and small and medium-sized businesses. The majority of the revenue for both FDL and CoBiz Insurance is derived from insurance product sales and referrals, and are paid by third-party insurance carriers. Insurance commissions are normally calculated as a percentage of the premium paid by our clients to the insurance carrier, and are paid to us by the insurance carrier for distributing and servicing their insurance products.

Corporate support and other consists of activities that are not directly attributable to the other reportable segments. Included in this category are primarily the activities of Leasing and the Parent.

The financial information for each business segment reflects that information which is specifically identifiable or which is allocated based on an internal allocation method. Results of operations and selected financial information by operating segment are as follows:

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	For the three months ended September 30, 2006						
	Colorado Business Bank	Arizona Business Bank	Investment banking services	Investment advisory and trust	Insurance	Corporate support and other	Consolidated
	(dollars in thousands)						
<i>Income Statement</i>							
Total interest income	\$ 25,817	\$ 9,816	\$ 34	\$ 5	\$ 2	\$ 85	\$ 35,759
Total interest expense	11,831	2,329			4	1,431	15,595
Net interest income	13,986	7,487	34	5	(2)	(1,346)	20,164
Provision for loan and credit losses	(60)	150				(15)	75
Net interest income after provision for loan and credit losses	14,046	7,337	34	5	(2)	(1,331)	20,089
Noninterest income	1,251	418	1,063	1,030	3,525	(4)	7,283
Noninterest expense	2,788	2,462	1,135	885	3,005	7,212	17,487
Income before income taxes	12,509	5,293	(38)	150	518	(8,547)	9,885
Provision for income taxes	4,556	2,002	(8)	58	210	(3,189)	3,629
Net income before management fees and overhead allocations	\$ 7,953	\$ 3,291	\$ (30)	\$ 92	\$ 308	\$ (5,358)	\$ 6,256
Management fees and overhead allocations, net of tax	2,934	1,072	38	43	79	(4,166)	
Net income	\$ 5,019	\$ 2,219	\$ (68)	\$ 49	\$ 229	\$ (1,192)	\$ 6,256

	For the nine months ended September 30, 2006						
<i>Income Statement</i>							
Total interest income	\$ 72,641	\$ 26,823	\$ 49	\$ 16	\$ 10	\$ 160	\$ 99,699
Total interest expense	31,143	5,959			4	4,008	41,114
Net interest income	41,498	20,864	49	16	6	(3,848)	58,585
Provision for loan and credit losses	915	298				(51)	1,162
Net interest income after provision for loan and credit losses	40,583	20,566	49	16	6	(3,797)	57,423
Noninterest income	3,376	1,138	4,118	3,054	9,088	68	20,842
Noninterest expense	8,303	7,035	3,322	2,632	8,185	21,429	50,906
Income before income taxes	35,656	14,669	845	438	909	(25,158)	27,359
Provision for income taxes	13,088	5,507	338	175	379	(9,469)	10,018
Net income before management fees and overhead allocations	\$ 22,568	\$ 9,162	\$ 507	\$ 263	\$ 530	\$ (15,689)	\$ 17,341
Management fees and overhead allocations, net of tax	8,611	3,167	119	136	244	(12,277)	
Net income	\$ 13,957	\$ 5,995	\$ 388	\$ 127	\$ 286	\$ (3,412)	\$ 17,341

	At September 30, 2006						
<i>Balance Sheet</i>							
Total assets	\$ 1,445,799	\$ 645,970	\$ 8,170	\$ 5,988	\$ 21,822	\$ 2,719	\$ 2,130,468
Total gross loans	\$ 980,140	\$ 536,309	\$	\$	\$	\$ 45	1,516,494

As of December 31, 2005, and September 30, 2006, the Company's intangible assets and related accumulated amortization were \$1,116,494 and \$1,116,494, respectively.

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Total deposits and
customer repurchase
agreements

\$ 1,318,720	\$ 323,130	\$	\$ 833	\$	1,642,683
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	For the three months ended September 30, 2005						
	Colorado Business Bank	Arizona Business Bank	Investment banking services	Investment advisory and trust	Insurance	Corporate support and other	Consolidated
	(dollars in thousands)						
<i>Income Statement</i>							
Total interest income	\$ 19,757	\$ 7,216	\$ 4	\$ 3	\$	\$ 31	\$ 27,011
Total interest expense	6,424	1,293				995	8,712
Net interest income	13,333	5,923	4	3		(964)	18,299
Provision for loan losses	463	434				(50)	847
Net interest income after provision for loan losses	12,870	5,489	4	3		(914)	17,452
Noninterest income	1,043	293	727	978	2,389		5,430
Noninterest expense	3,040	2,197	877	867	2,384	5,878	15,243
Income before income taxes	10,873	3,585	(146)	114	5	(6,792)	7,639
Provision for income taxes	3,815	1,341	(55)	46	7	(2,559)	2,595
Net income before management fees and overhead allocations	\$ 7,058	\$ 2,244	\$ (91)	\$ 68	\$ (2)	\$ (4,233)	\$ 5,044
Management fees and overhead allocations, net of tax	2,433	731	32	38	61	(3,295)	
Net income	\$ 4,625	\$ 1,513	\$ (123)	\$ 30	\$ (63)	\$ (938)	\$ 5,044

	For the nine months ended September 30, 2005						
<i>Income Statement</i>							
Total interest income	\$ 56,008	\$ 18,539	\$ 14	\$ 10	\$ 19	\$ 113	\$ 74,703
Total interest expense	15,923	3,367				3,161	22,451
Net interest income	40,085	15,172	14	10	19	(3,048)	52,252
Provision for loan losses	1,153	969				(180)	1,942
Net interest income after provision for loan losses	38,932	14,203	14	10	19	(2,868)	50,310
Noninterest income	3,204	893	2,696	2,947	7,721	3	17,464
Noninterest expense	9,796	6,796	2,471	2,583	6,904	17,006	45,556
Income before income taxes	32,340	8,300	239	374	836	(19,871)	22,218
Provision for income taxes	11,721	3,076	95	150	336	(7,436)	7,942
Net income before management fees and overhead allocations	\$ 20,619	\$ 5,224	\$ 144	\$ 224	\$ 500	\$ (12,435)	\$ 14,276
Management fees and overhead allocations, net of tax	6,828	2,058	97	114	185	(9,282)	
Net income	\$ 13,791	\$ 3,166	\$ 47	\$ 110	\$ 315	\$ (3,153)	\$ 14,276

	At September 30, 2005						
<i>Balance Sheet</i>							
Total assets	\$ 1,305,102	\$ 524,916	\$ 6,376	\$ 5,315	\$ 20,073	\$ 2,736	\$ 1,864,518
Total gross loans	854,627	415,791				73	1,270,491
Total deposits and customer repurchase agreements	1,166,010	290,445		880			1,457,335

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This discussion should be read in conjunction with our consolidated financial statements and notes thereto included in this Form 10-Q. Certain terms used in this discussion are defined in the notes to these financial statements. For a description of our accounting policies, see Note 1 of Notes to Consolidated Financial Statements included in our Form 10-K for the year ended December 31, 2005. For a discussion of the segments included in our principal activities, see Note 10 to these financial statements.

As of December 31, 2005, and September 30, 2006, the Company's intangible assets and related accumulated amortization were \$1.2 million and \$1.2 million, respectively.

Executive Summary

The Company is a financial holding company that offers a broad array of financial service products to its target market of small and medium-sized businesses and high-net-worth individuals. Our operating segments include our commercial banking franchise, Colorado Business Bank and Arizona Business Bank; investment banking services; investment advisory and trust services; and insurance services.

Earnings are derived primarily from our net interest income, which is interest income less interest expense, and our noninterest income earned from our fee-based business lines and banking service fees, offset by noninterest expense. As the majority of our assets are interest-earning and our liabilities are interest-bearing, changes in interest rates impact our net interest margin, the largest component of our

operating revenue (which is defined as net interest income plus non-interest income). We manage our interest-earning assets and interest-bearing liabilities to reduce the impact of interest rate changes on our operating results. We also have focused on reducing our dependency on our net interest margin by increasing our noninterest income.

Our Company has focused on developing an organization with personnel, management systems and products that will allow us to compete effectively and position us for growth. The cost of this process relative to our size has been high. In addition, we have operated with excess capacity during the start-up phases of various projects. As a result, relatively high levels of non-interest expense have adversely affected our earnings over the past several years. Salaries and employee benefits comprised most of this overhead category. However, we believe that our compensation levels have allowed us to recruit and retain a highly qualified management team capable of implementing our business strategies. We believe our compensation policies, which include the granting of options to purchase common stock to many employees and the offering of an employee stock purchase plan, have highly motivated our employees and enhanced our ability to maintain customer loyalty and generate earnings.

Financial Highlights

- Net income for the three and nine months ended September 30, 2006 were \$6.3 million and \$17.3 million respectively, compared to \$5.0 million and \$14.3 million for the same periods in 2005.
- Diluted earnings per share for the three and nine months ended September 30, 2006 was \$0.27 and \$0.74, compared to \$0.22 and \$0.62 for the same periods in 2005.
- Net interest income on a tax-equivalent basis for the three and nine months ended September 30, 2006 increased to \$20.3 million and \$59.0 million respectively, compared to \$18.4 million and \$52.6 million for the same periods in 2005.
- The net interest margin on a tax-equivalent basis was 4.14% and 4.19% for the three and nine months ended September 30, 2006, respectively, compared to 4.30% and 4.25% for the same periods in 2005.
- Gross loans increased 13.8% from December 31, 2005, or 18.4% on an annualized basis.
- Asset quality remained strong at the end of the second quarter, with non-performing assets as a percentage of total assets at 0.03%, down slightly from 0.04% from the prior year's third quarter.
- Noninterest income as a percentage of operating revenues increased to 26.53% and 26.24% for the three and nine months ending September 30, 2006, compared to 22.88% and 25.05% for the same periods in 2005.

Critical Accounting Policies

The Company's discussion and analysis of its financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. In making those critical accounting estimates, we are required to make assumptions about matters that are highly uncertain at the time of the estimate.

Different estimates we could reasonably have used, or changes in the assumptions that could occur, could have a material effect on our financial condition or results of operations. A description of our critical accounting policies was provided in the Management's Discussion and Analysis of Financial Condition and Results of Operation section of our Annual Report on Form 10-K for the year ended December 31, 2005. There have been no changes in our critical accounting policies and no other significant changes to the assumptions and estimates related to them, except for the adoption of SFAS 123(R) during the quarter ended March 31, 2006.

Under SFAS 123(R), we use the Black-Scholes option valuation model to determine the fair value of our stock options. The Black-Scholes fair value model includes various assumptions, including the expected volatility, expected life, and expected dividend rate of the options. In addition, the Company is required to estimate the amount of options issued that are expected to be forfeited. These assumptions reflect our best estimates, but they involve inherent uncertainties based on market conditions generally outside of our control. As a result, if other assumptions had been used, stock-based compensation expense, as calculated and recorded under SFAS 123(R), could have been materially impacted. Furthermore, if we use different assumptions in future periods, stock-based compensation expense could be materially impacted in future periods.

Financial Condition

Total assets increased by \$197.4 million to \$2.1 billion as of September 30, 2006, from \$1.9 billion as of December 31, 2005. The increase in total assets is primarily due to growth in net loans which were largely funded by the Company's wholesale borrowing sources.

Investments. Total investments increased \$3.7 million to \$469.9 million, from \$466.2 million as of December 31, 2005. The increase in investments was due to the purchase of additional stock in the Federal Home Loan Bank (FHLB) in order to expand the Company's borrowing base. The FHLB functions as a source of credit to the Company. As a member of the FHLB system, the Company has access to credit advances that are limited to a percentage of the amount of FHLB stock owned by the Company.

The following table sets forth the balance of loans and deposits as of September 30, 2006, December 31, 2005 and September 30, 2005 (dollars in thousands):

	September 30, 2006		December 31, 2005		September 30, 2005	
	Amount	% of Portfolio	Amount	% of Portfolio	Amount	% of Portfolio
LOANS						
Commercial	\$ 451,593	30.1	% \$ 421,497	32.0	% \$ 412,121	32.9
Real Estate - mortgage	706,749	47.2	% 682,503	51.9	% 647,614	51.6
Real Estate - construction	280,437	18.7	% 150,680	11.5	% 135,585	10.8
Consumer	64,269	4.3	% 65,932	5.0	% 63,108	5.0
Other	13,446	0.9	% 12,056	0.9	% 12,063	1.0
Gross loans	1,516,494	101.2	% 1,332,668	101.3	% 1,270,491	101.3
Less allowance for loan losses	(17,715)	(1.2)(16,906)	(1.3)(16,440)	(1.3
Net loans	\$ 1,498,779	100.0	% \$ 1,315,762	100.0	% \$ 1,254,051	100.0

	September 30, 2006		December 31, 2005		September 30, 2005	
	Amount	% of Portfolio	Amount	% of Portfolio	Amount	% of Portfolio
DEPOSITS AND CUSTOMER REPURCHASE AGREEMENTS						
NOW and money market accounts	\$ 500,262	30.5	% \$ 502,283	32.5	% \$ 470,358	32.3
Savings	11,304	0.7	% 8,461	0.5	% 9,632	0.7
Certificates of deposits under \$100,000	70,850	4.3	% 81,436	5.3	% 87,114	6.0
Certificates of deposits \$100,000 and over	376,350	22.9	% 298,681	19.3	% 311,567	21.4
Total interest-bearing deposits	958,766	58.4	% 890,861	57.7	% 878,671	60.3
Noninterest-bearing demand deposits	437,571	26.6	% 436,091	28.3	% 433,787	29.8
Customer repurchase agreements	246,346	15.0	% 216,725	14.0	% 144,877	9.9
Total deposits and customer repurchase agreements	\$ 1,642,683	100.0	% \$ 1,543,677	100.0	% \$ 1,457,335	100.0

Loans. Gross loans increased by \$183.8 million to \$1.5 billion as of September 30, 2006, from \$1.3 billion at December 31, 2005. The increase in loans is primarily due to growth in our real estate construction and mortgage portfolios. The growth has been evenly distributed between Colorado and Arizona, with the two markets accounting for 48% and 52% of the growth since December 31, 2005, respectively.

Goodwill. Goodwill increased by \$0.5 million to \$39.0 million at September 30, 2006, from \$38.4 million at December 31, 2005. The increase was due to additional purchase price consideration paid to the former owners of Alexander Capital Management Group, Inc. under the terms of an earn-out agreement for the twelve months ending March 31, 2006.

Other Assets. Other Assets increased \$1.6 million to \$11.0 million at September 30, 2006, from \$9.5 million at December 31, 2005. The increase was primarily comprised of \$1.7 million due to the consolidation of a small investment partnership upon the adoption of EITF 04-05 and a \$1.5 million capital contribution to an investment fund to which the Company has committed to invest. These increases were offset by a decrease in fee-based accounts receivable and other miscellaneous assets.

Deposits. Deposits increased by \$69.4 million to \$1.4 billion as of September 30, 2006, from \$1.3 billion as of December 31, 2005. The increase in deposits was primarily due to the initiation and utilization of brokered certificates of deposits (CDs) as an additional wholesale funding source. As of September 30, 2006, the Company had brokered CDs of \$86.3 million. There were no brokered CDs outstanding as of December 31, 2005. Brokered CDs offer an additional option for obtaining funds at competitive prices without the collateral requirements other traditional sources require, such as FHLB advances. In 2006, the Company has experienced high volatility in its customer deposit base. Core-deposit growth has been a challenge due to increased competition from both other banks and financial service

providers.

Securities Sold Under Agreements to Repurchase. Securities sold under agreements to repurchase increased \$29.6 million to \$246.3 million at September 30, 2006, from \$216.7 million at December 31, 2005.

Securities sold under agreement to repurchase are represented by two types, customer repurchase agreements and street repurchase agreements. Management does not consider customer repurchase agreements to be a wholesale funding source, but rather an additional treasury management service provided to our customer base. As of September 30, 2006 and December 31, 2005, all of our repurchase agreements were transacted on behalf of our customers. Our customer repurchase agreements are based on an overnight investment sweep that can fluctuate based on our customers' operating account balances.

Other Short-Term Borrowings. Other short-term borrowings increased \$76.4 million to \$241.4 million at September 30, 2006, from \$165.0 million at December 31, 2005. Other short-term borrowings consist of fed funds purchased, overnight and term borrowings from the FHLB, and short-term borrowings from the U.S. Treasury. Other short-term borrowings are used as part of our liquidity management strategy and can fluctuate based on the Company's cash position. The Company's wholesale funding needs are largely dependent on core deposit levels, which have proven to be more volatile due to increased competition and rising rates. If we are unable to maintain deposit balances at a level sufficient to fund our asset growth, our composition of interest-bearing liabilities will shift toward additional wholesale funds, which typically have a higher interest cost than our core deposits.

Accrued Interest and Other Liabilities. Accrued interest and other liabilities increased \$2.9 million to \$18.6 million at September 30, 2006, from \$15.7 million at December 31, 2005. The increase was primarily driven by a \$1.7 million increase in a minority interest due to the consolidation of a small investment partnership, the establishment of a \$0.6 million reserve for letters of credit losses and a \$0.5 million increase in accrued interest on junior subordinated debentures.

Results of Operations

Overview

The following table presents the condensed statements of income for the three and nine months ended September 30, 2006 and 2005.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
	(dollars in thousands)		(dollars in thousands)	
INCOME STATEMENT DATA				
Interest income	\$ 35,759	\$ 27,011	\$ 99,699	\$ 74,703
Interest expense	15,595	8,712	41,114	22,451
NET INTEREST INCOME BEFORE PROVISION	20,164	18,299	58,585	52,252
Provision for loan and credit losses	75	847	1,162	1,942
NET INTEREST INCOME AFTER PROVISION	20,089	17,452	57,423	50,310
Noninterest income	7,283	5,430	20,842	17,464
Noninterest expense	17,487	15,243	50,906	45,556
INCOME BEFORE INCOME TAXES	9,885	7,639	27,359	22,218
Provision for income taxes	3,629	2,595	10,018	7,942
NET INCOME	\$ 6,256	\$ 5,044	\$ 17,341	\$ 14,276

Annualized return on average assets for the three and nine months ended September 30, 2006 was 1.18% and 1.14%, respectively, compared to 1.08% and 1.07% for the same periods in 2005. Annualized return on average common shareholders' equity for the three and nine months ended September 30, 2006 was 16.60% and 16.10%, compared to 14.90% and 14.88% for the same periods in 2005. The increase in our return on average equity ratio is the result of net income growing at a faster rate than equity. The increase in net income is primarily attributable to continued growth in our net interest earning assets. The growth in equity is impacted not only by our net income, but also by the issuance of stock for option exercises and earn-out arrangements as well as fluctuations in the market values of our available-for-sale investments and cash flow hedges.

Net Interest Income. The largest component of our net income is our net interest income. Net interest income is the difference between interest income, principally from loans and investment securities, and interest expense, principally on customer deposits and borrowings. Changes in net interest income result from changes in volume, net interest spread and net interest margin. Volume refers to the average dollar levels of interest-earning assets and interest-bearing liabilities. Net interest spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities. Net interest margin refers to net interest income divided by average interest-earning assets and is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities.

As the majority of our assets are interest-earning and our liabilities are interest-bearing, changes in interest rates may impact our net interest margin. Rising short-term rates and the flattening of the yield curve has compressed interest rate spreads and dampened expansion of the net interest margin as our wholesale borrowing costs increase and our ability to raise lending rates is limited. The target federal funds rate increased 150 basis points as of September 30, 2006 over the same period in 2005, significantly increasing our wholesale funding costs. Conversely, nominal increases for the same period on the yields of five and ten year treasury securities has negatively impacted our growth in interest income from our investment portfolio and fixed rate loan portfolio. Additionally, there have been a number of new bank entrants and an expansion of existing bank franchises within the Colorado and Arizona markets. This has increased competition in both loan and deposit pricing, which has led to the stabilization of our net interest margin.

The following tables set forth the average amounts outstanding for each category of interest-earning assets and interest-bearing liabilities, the interest earned or paid on such amounts, and the average rate earned or paid for the three and nine months ended September 30, 2006 and 2005.

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	For the three months ended September 30, 2006				2005			
	Average Balance (dollars in thousands)	Interest earned or paid	Average yield or cost (1)		Average Balance	Interest earned or paid	Average yield or cost (1)	
Assets								
Federal funds sold and other	\$ 7,068	\$ 120	6.64	%	\$ 2,750	\$ 48	6.83	%
Investment securities (2)	476,049	5,595	4.60	%	479,920	4,616	3.76	%
Loans (2), (3)	1,480,819	30,172	7.97	%	1,232,413	22,448	7.13	%
Allowance for loan losses	(17,524)				(15,979)			
Total interest earning assets	\$ 1,946,412	\$ 35,887	7.21	%	\$ 1,699,104	\$ 27,112	6.24	%
Noninterest-earning assets								
Cash and due from banks	46,342				47,869			
Other	106,671				98,255			
Total assets	\$ 2,099,425				\$ 1,845,228			
Liabilities and Shareholders								
Equity								
Deposits								
NOW and money market deposits	\$ 508,351	\$ 3,611	2.82	%	\$ 458,639	\$ 2,071	1.79	%
Savings deposits	10,319	32	1.23	%	10,195	11	0.43	%
Certificates of deposits								
Under \$100,000	75,258	796	4.20	%	85,301	639	2.97	%
\$100,000 and over	384,684	4,584	4.73	%	308,218	2,412	3.10	%
Total Interest-bearing deposits	\$ 978,612	\$ 9,023	3.66	%	\$ 862,353	\$ 5,133	2.36	%
Other borrowings								
Securities sold under agreements to repurchase and other short-term borrowings								
	454,215	5,134	4.42	%	342,351	2,583	2.95	%
Junior subordinated debentures	72,166	1,438	7.80	%	64,994	996	6.00	%
Total interest-bearing liabilities	\$ 1,504,993	\$ 15,595	4.09	%	\$ 1,269,698	\$ 8,712	2.71	%
Noninterest-bearing demand accounts								
	425,798				429,100			
Total deposits and interest-bearing liabilities	1,930,791				1,698,798			
Other noninterest-bearing liabilities	19,033				12,089			
Total liabilities and preferred securities	1,949,824				1,710,887			
Shareholders equity	149,601				134,341			
Total liabilities and shareholders equity	\$ 2,099,425				\$ 1,845,228			
Net interest income		\$ 20,292				\$ 18,400		
Net interest spread			3.12	%			3.53	%
Net interest margin			4.14	%			4.30	%
Ratio of average interest-earning assets to average interest-bearing liabilities								
	129.33	%			133.82	%		

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	For the nine months ended September 30, 2006			2005		
	Average Balance (dollars in thousands)	Interest earned or paid	Average yield or cost (1)	Average Balance	Interest earned or paid	Average yield or cost (1)
Assets						
Federal funds sold and other	\$ 6,275	\$ 297	6.32%	\$ 3,629	\$ 166	6.12%
Investment securities (2)	471,454	15,992	4.54%	485,557	13,633	3.75%
Loans (2), (3)	1,420,812	83,792	7.88%	1,178,780	61,226	6.94%
Allowance for loan losses	(17,224)			(15,380)		
Total interest earning assets	\$ 1,881,317	\$ 100,081	7.11%	\$ 1,652,586	\$ 75,025	6.07%
Noninterest-earning assets						
Cash and due from banks	47,135			40,978		
Other	103,330			93,679		
Total assets	\$ 2,031,782			\$ 1,787,243		
Liabilities and Shareholders Equity						
Deposits						
NOW and money market deposits	\$ 510,395	\$ 10,034	2.63%	\$ 451,824	\$ 4,837	1.43%
Savings deposits	8,994	61	0.91%	10,878	30	0.37%
Certificates of deposits						
Under \$100,000	79,151	2,317	3.91%	82,778	1,691	2.73%
\$100,000 and over	346,150	11,227	4.34%	280,502	5,834	2.78%
Total interest-bearing deposits	\$ 944,690	\$ 23,639	3.35%	\$ 825,982	\$ 12,392	2.01%
Other borrowings						
Securities sold under agreements to repurchase and other short-term borrowings	427,764	13,453	4.20%	356,696	6,840	2.56%
Junior subordinated debentures	72,166	4,022	7.45%	69,346	3,219	6.21%
Total interest-bearing liabilities	\$ 1,444,620	\$ 41,114	3.80%	\$ 1,252,024	\$ 22,451	2.40%
Noninterest-bearing demand accounts	427,058			394,963		
Total deposits and interest-bearing liabilities	1,871,678			1,646,987		
Other noninterest-bearing liabilities	16,139			12,001		
Total liabilities and preferred securities	1,887,817			1,658,988		
Shareholders equity	143,965			128,255		
Total liabilities and shareholders equity	\$ 2,031,782			\$ 1,787,243		
Net interest income		\$ 58,967			\$ 52,574	
Net interest spread			3.31%			3.67%
Net interest margin			4.19%			4.25%
Ratio of average interest-earning assets to average interest-bearing liabilities	130.23%			131.99%		

-
- (1) Average yield or cost for the three and nine months ended September 30, 2006 and 2005 has been annualized and is not necessarily indicative of results for the entire year.
 - (2) Yields include adjustments for tax-exempt interest income based on the Company's effective tax rate.
 - (3) Loan fees included in interest income are not material. Nonaccrual loans are included in average loans outstanding.

The increase in interest income on a tax-equivalent basis for the three and nine months ended September 30, 2006 was primarily driven by an increase in the average volume of our interest-earning assets. The volume of our interest-earning assets increased due to the growth in our average loan portfolio of \$248.4 million and \$242.0 million for the three and nine months ended September 30, 2006. To a lesser extent, the yield on interest-earning assets also contributed to the increase, as the average yield increased 97 basis points and 104 basis points for the three and nine months ended September 30, 2006. Since September 30, 2005, the prime rate has increased from 6.75% to 8.25%, which has positively impacted net interest income as a large portion of our loan portfolio adjusts simultaneously with movements in the prime rate.

The increase in interest expense is attributed primarily to the rising interest rate environment and to a lesser extent the increased volume of interest-bearing liabilities. The rates on our deposit portfolio and

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wholesale funding sources are significantly impacted by changes in short-term rates, in addition to other economic factors. Since September 2005 short-term LIBOR and the federal funds rates have increased approximately 150 basis points, which have increased the funding costs of our deposit and wholesale borrowing portfolios. Additionally, core deposit growth has been relatively muted, causing a greater reliance on wholesale borrowings to meet our funding needs. Higher levels of wholesale funding sources typically increases interest expense as wholesale funds bear a higher interest cost as compared with core deposits.

Our net interest income is driven almost exclusively by our core banking franchise. Future increases in net interest income will primarily come by increasing our loan and investment portfolios, offset by the cost of funds from growth in our deposit portfolio and other funding sources. We expect to continue augmenting the organic growth from our existing banks with the addition of new de novo banks in Arizona and Colorado as qualified bank presidents are identified.

Noninterest Income. The following table presents noninterest income for the three and nine months ended September 30, 2006 and 2005 (dollars in thousands):

	Three months ended September 30,				Nine Months ended September 30,			
	2006	2005	Increase/(decrease) Amount	%	2006	2005	Increase/(decrease) Amount	%
<i>NONINTEREST INCOME</i>								
Deposit service charges	\$ 679	\$ 678	\$ 1	0	% \$ 2,104	\$ 2,150	\$ (46)	(2)%
Other loan fees	186	196	(10)	(5)%	555	542	13	2 %
Investment advisory and trust income	1,030	978	52	5 %	3,054	2,947	107	4 %
Insurance income	3,525	2,389	1,136	48 %	9,088	7,721	1,367	18 %
Investment banking income	1,063	727	336	46 %	4,118	2,696	1,422	53 %
Other income	800	462	338	73 %	1,923	1,408	515	37 %
Total noninterest income	\$ 7,283	\$ 5,430	\$ 1,853	34 %	\$ 20,842	\$ 17,464	\$ 3,378	19 %

Noninterest income includes revenues earned from sources other than interest income. These sources include: service charges and fees on deposit accounts, letter of credit and ancillary loan fees, income from investment advisory and trust services, income from life insurance and wealth transfer products, benefits brokerage, property and casualty insurance, retainer and success fees from investment banking engagements, increases in the cash surrender value of bank-owned life insurance, and net gains on sales of investment securities and other assets.

Deposit Service Charges. Deposit service charges primarily consist of fees earned from our treasury management services where customers are billed for deposits on analysis. Gross fees for services billed on analysis have increased 33% for the three and nine months ended September 30, 2006, compared to the same periods in 2005. Customers are given the option to pay for these services in cash or by offsetting the fees for these services against an earnings credit that is given for maintaining noninterest-bearing deposits. Although the average balance of deposits tied to our treasury management services has increased 13% in 2006 compared to 2005, the earnings credit rate (rate credited to our customers based on deposit balances to offset treasury management charges) has also increased due to an increase in the U.S. Treasury rates which is used as a benchmark for the earnings credit rate. The increase in the earnings credit rate has slightly decreased our treasury management fees for the nine months ended September 30, 2006, compared to the same period in 2005. Other miscellaneous deposit charges are transactional by nature and may not be consistent period-over-period.

Investment Advisory and Trust Income. Investment advisory and trust income for the three and nine months ended September 30, 2006 increased slightly due to a modest increase in the overall assets under management from September 30, 2005 to September 30, 2006. As of September 30, 2006, ACMG and PAM had a combined \$602.6 million in discretionary assets under management, an 11% increase over

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September 30, 2005, and \$114.5 million in non-discretionary assets under management, a 20% decrease over September 30, 2005.

Insurance Income. Insurance income is derived from three main areas, wealth transfer, benefits consulting and property and casualty. The majority of fees earned on wealth transfer transactions are earned at the inception of the product offering in the form of commissions. As the fees on these products are transactional by nature, fee income can fluctuate from period-to-period based on the number of transactions that have been closed. Revenue from benefits consulting and property and casualty is a more recurring revenue source. For the three and nine months ended September 30, 2006, insurance income increased 48% and 18% when compared to the three and nine months ended September 30, 2005. The Company expanded the number of producers in all areas of its insurance operations during the latter part of 2005 and expects the segment to show continued growth, particularly in the benefits consulting and property and casualty areas.

For the three and nine months ended on September 30, 2006 and 2005, revenue earned from the Insurance segment is comprised of the following:

	Three months ended September 30, 2006		2005		Nine months ended September 30, 2006		2005	
Wealth transfer and executive compensation	60.89	%	41.20	%	53.74	%	47.41	%
Benefits consulting	22.07	%	28.89	%	24.55	%	26.38	%
Property and casualty	14.98	%	25.65	%	19.27	%	23.78	%
Fee income	2.06	%	4.26	%	2.44	%	2.43	%
	100.00	%	100.00	%	100.00	%	100.00	%

Investment Banking Income. Investment banking income includes retainer fees which are recognized over the expected term of the engagement and success fees which are recognized when the transaction is completed and collectibility of fees is reasonably assured. Investment banking income is transactional by nature and will fluctuate based on the number of clients engaged and transactions successfully closed. The increase in revenue for the first nine months of 2006 compared to 2005 was due primarily to the size of transactions completed in 2006, with one transaction accounting for \$1.6 million in revenue.

Other Income. Other income is comprised of increases in the cash surrender value of BOLI, earnings on equity method investments, merchant charges, bankcard fees, wire transfer fees, foreign exchange fees, and safe deposit income. The increase in other income for the first nine months of 2006 compared to 2005 was primarily due to an increase in earnings from equity investments and the cash surrender value of BOLI, in addition to fees generated from the customer hedging program.

We believe offering such complementary products as discussed above allows us to both broaden our relationships with existing customers and attract new customers to our core business. We believe the fees generated by these services will increase our noninterest income and eventually reduce our dependency on net interest income. Noninterest income as a percentage of operating revenues was 26.5% and 26.2% for the three and nine months ended September 30, 2006, compared to 22.9% and 25.1% for the same periods in 2005. This level of noninterest income to operating revenues is consistent with the Company's on-going goal of diversifying our revenue and reducing our dependency on net interest income.

Noninterest Expense

The following table presents noninterest expense for the three and nine months ended September 30, 2006 and 2005 (dollars in thousands):

	Three months ended September 30,				Nine Months ended September 30,					
	2006 (dollars in thousands)	2005	Increase/(decrease) Amount	%	2006	2005	Increase/(decrease) Amount	%		
NONINTEREST EXPENSES										
Salaries and employee benefits	\$11,855	\$9,795	\$2,060	21	%	\$34,219	\$29,141	\$5,078	17	%
Occupancy expenses, premises and equipment	2,961	2,814	147	5	%	8,517	8,181	336	4	%
Amortization of intangibles	118	137	(19)	(14))%	355	416	(61)	(15))%
Other operating expenses	2,506	2,484	22	1	%	7,742	7,679	63	1	%
Loss on sale of other assets and securities	47	13	34	262	%	73	139	(66)	(47))%
Total noninterest expenses	\$17,487	\$15,243	\$2,244	15	%	\$50,906	\$45,556	\$5,350	12	%

Salaries and Employee Benefits. Salaries and employee benefits for the three and nine months ended September 30, 2006 have increased primarily due to the growth of our full time equivalent employee base. As of September 30, 2006, the Company employed 460 full time equivalent employees compared to 431 at September 30, 2005. The growth in full time equivalent employees is due to the expansion of our de novo banks and organic growth of existing operations. The annual cost of living and performance raises awarded to employees effective January 1, 2006, which averaged 4.58%, have also contributed to the increase. Also included in salaries and employee benefits is \$0.3 million and \$0.9 million related to stock-based compensation due to the adoption of SFAS 123(R) for the three and nine months ended September 30, 2006, respectively. Under the prior accounting rules in place during 2005, the Company did not recognize any expense related to stock-based compensation. Another contributor to the increase in salary and benefit costs was the variable compensation associated with increased investment banking and insurance revenues during the three and nine months ending September 30, 2006 as compared to the same periods in 2005. Bonuses related to investment banking and insurance transactions increased \$0.2 and \$0.7 million for the three and nine months ending September 30, 2006, when compared to the same periods in 2005.

Occupancy Costs. Occupancy costs consist primarily of rent, depreciation, utilities, property taxes and insurance. Occupancy costs for the first nine months of 2006 have remained relatively stable when compared to the same period in 2005, as the majority of our de novo locations were in place as of September 30, 2005. The slight increase is primarily due to depreciation from the expansion of several existing locations and increases in common area management charges.

Other Operating Expenses. Other operating expenses consist primarily of business development expenses (meals, entertainment and travel), charitable donations, professional services (auditing, legal, marketing and courier) and regulatory assessments. For the three and nine months ended September 30, 2006, other operating expenses were stable with the same periods in 2005.

Provision and Allowance for Loan and Credit Losses

The provision for loan and credit losses was \$0.1 million and \$1.2 million for the three and nine months ended September 30, 2006, compared to \$0.8 million and \$1.9 million for the same periods in 2005. For the first nine months of 2006, the Company had net recoveries of \$0.2 million compared with net charge-offs of \$0.2 million for the first nine months of 2005. As of September 30, 2006, the allowance for loan and credit losses amounted to 1.21% of total loans, compared to 1.29% at September 30, 2005. The Company's percentage of non-performing assets to total assets decreased to 3 basis points as of September 30, 2006 from 4 basis points in 2005. The decrease in the provision for loan and credit losses

for the three and nine months ended September 30, 2006, is due to the increase in the allowance for loan losses through net loan recoveries and the overall improvement in our credit quality measures.

The allowance for loan losses represents management's recognition of the risks of extending credit and its evaluation of the quality of the loan portfolio. The allowance is maintained to provide for probable losses related to specifically identified loans and for losses inherent in the loan portfolio that have been incurred as of the balance sheet date. The allowance is based on various factors affecting the loan portfolio, including a review of problem loans, business conditions, historical loss experience, evaluation of the quality of the underlying collateral, and holding and disposal costs. The allowance is increased by additional charges to operating income and reduced by loans charged off, net of recoveries.

The allowance for credit losses represents management's recognition of a separate reserve for off-balance sheet loan commitments and letters of credit. While the allowance for loan losses is recorded as a contra-asset to the loan portfolio on the consolidated balance sheet, the allowance for credit losses is recorded in Accrued Interest and Other Liabilities in the accompanying consolidated balance sheet. Although the allowances are presented separately on the balance sheet, any losses incurred from credit losses would be reported as a charge-off in the allowance for loan losses, since any loss would be recorded after the off-balance sheet commitment had been funded. Due to the relationship of these allowances, as extensions of credit underwritten through a comprehensive risk analysis, information on both the allowance for loan and credit losses positions is presented in the following table.

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	Nine months ended September 30, 2006 (in thousands)	Year ended December 31, 2005	Nine months ended September 30, 2005
Allowance for loan losses at beginning of period	\$ 16,906	\$ 14,674	\$ 14,674
Charge-offs:			
Commercial	(262)	(363)	(325)
Real estate mortgage	(1)	(246)	(246)
Consumer	(25)	(99)	(41)
Total charge-offs	(288)	(708)	(612)
Recoveries:			
Commercial	486	104	72
Real estate mortgage	25	277	271
Consumer	1	94	93
Total recoveries	512	475	436
Net charge-offs	224	(233)	(176)
Provisions for loan losses charged to operations	585	2,465	1,942
Allowance for loan losses at end of period	\$ 17,715	\$ 16,906	\$ 16,440
Allowance for credit losses at beginning of period	\$	\$	\$
Provisions for credit losses charged to operations	577		
Allowance for credit losses at end of period	\$ 577	\$	\$
Total provision for loan and credit losses	\$ 1,162	\$ 2,465	\$ 1,942
Ratio of net recoveries (charge-offs) to average loans (1)	0.02 %	(0.02)%	(0.02)%
Average loans outstanding during the period	\$ 1,420,812	\$ 1,209,377	\$ 1,178,780

(1) The ratios for the nine months ended September 30, 2006 and 2005 have been annualized and are not necessarily indicative of the results for the entire year.

Nonperforming Assets

Nonperforming assets consist of nonaccrual loans, restructured loans, past due loans, repossessed assets, and other real estate owned. The following table presents information regarding nonperforming assets as of the dates indicated:

	At September 30, 2006 (dollars in thousands)		At December 31, 2005		At September 30, 2005	
Nonperforming Loans						
Loans 90 days or more delinquent and still accruing	\$	196	\$		\$	225
Nonaccrual loans		448		907		480
Total nonperforming loans		644		907		705
Reposessed assets						6
Total nonperforming assets	\$	644	\$	907	\$	711
Allowance for loan and credit losses	\$	18,292	\$	16,906	\$	16,440
Ratio of nonperforming assets to total assets		0.03	%	0.05	%	0.04
Ratio of nonperforming loans to total loans		0.04	%	0.07	%	0.06
Ratio of allowance for loan and credit losses to total loans		1.21	%	1.27	%	1.29
Ratio of allowance for loan and credit losses to nonperforming loans		2840.37	%	1863.95	%	2331.91

Contractual Obligations and Commitments

Summarized below are the Company's contractual obligations (excluding deposit liabilities) to make future payments as of September 30, 2006:

	Within one year (dollars in thousands)	After one but within three years	After three but within five years	After five years	Total
Federal funds purchased	\$ 40,900	\$	\$	\$	\$ 40,900
TIO funds purchased	10,000				10,000
FHLB overnight funds purchased	90,500				90,500
Securities sold under agreements to repurchase	246,346				246,346
FHLB advances	99,973				99,973
Junior subordinated debentures				72,166	72,166
Operating lease obligations	4,645	8,910	6,371	4,778	24,704
Total contractual obligations	\$ 492,364	\$ 8,910	\$ 6,371	\$ 76,944	\$ 584,589

The Company has employed a strategy to expand its offering of fee-based products through the acquisition of entities that complement its business model. We will often structure the purchase price of an acquired entity to include an earn-out, which is a contingent payment based on achieving future performance levels. Given the uncertainty of today's economic climate and the performance challenges it creates for companies, we feel that the use of earn-outs in acquisitions is an effective method to bridge the expectation gap between a buyer's caution and a seller's optimism. Earn-outs help to protect buyers from paying a full valuation up-front without the assurance of the acquisition's performance, while allowing sellers to participate in the full value of the company provided the anticipated performance does occur. Since the earn-out payments are determined based on the acquired company's performance during the earn-out period, the total payments to be made are not known at the time of the acquisition. The Company has committed to make additional earn-out payments to the former shareholders of FDL based on earnings performance.

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The contractual amount of the Company's financial instruments with off-balance sheet risk expiring by period at September 30, 2006, is presented below:

	Within one year (dollars in thousands)	After one but within three years	After three but within five years	After five years	Total
Unfunded loan commitments	\$ 430,286	\$ 240,636	\$ 22,344	\$ 6,878	\$ 700,144
Standby letters of credit	37,480	3,861	5		41,346
Commercial letters of credit	5,604	682	4,303		10,589
Unfunded commitments for partnership interests	5,263				5,263
Company guarantees	4,848				4,848
Total commitments	\$ 483,481	\$ 245,179	\$ 26,652	\$ 6,878	\$ 762,190

The Company is party to financial instruments with off-balance sheet risk in the normal course of business to meet the liquidity, credit enhancement, and financing needs of its customers. These financial instruments include legally binding commitments to extend credit and standby letters of credit and involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheet. Credit risk is the principal risk associated with these instruments. The contractual amounts of these instruments represent the amount of credit risk should the instruments be fully drawn upon and the customer defaults.

To control the credit risk associated with entering into commitments and issuing letters of credit, the Company uses the same credit quality, collateral policies, and monitoring controls in making commitments and letters of credit as it does with its lending activities. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation.

Legally binding commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Standby letters of credit obligate the Company to meet certain financial obligations of its customers if, under the contractual terms of the agreement, the customers are unable to do so. The financial standby letters of credit issued by the Company are irrevocable. Payment is only guaranteed under these letters of credit upon the borrower's failure to perform its obligations to the beneficiary.

The Company has also entered into interest-rate swap agreements under which it is required to either receive cash or pay cash to a counterparty depending on changes in interest rates. The interest-rate swaps are carried at their fair value on the consolidated balance sheet with the fair value representing the net present value of expected future cash receipts or payments based on market interest rates as of the balance sheet date. Because the interest-rate swaps recorded on the balance sheet at September 30, 2006 do not represent amounts that will ultimately be received or paid under the contracts, they are excluded from the table above.

Liquidity and Capital Resources

Our primary source of shareholders' equity is the retention of our net after-tax earnings and proceeds from the issuance of common stock. At September 30, 2006, shareholders' equity totaled \$155.6 million, a \$19.1 million increase from December 31, 2005. The increase in shareholders' equity is primarily due to net income of \$17.3 million, \$2.3 million from the issuance of common stock from option exercises and the Company's employee stock purchase plan, \$1.6 million due to the accounting treatment of SFAS 123R, \$0.3 million from the issuance of common stock in the ACMG earn-out and \$1.2 increase in the tax-effected fair value of available-for-sale securities and derivative instruments. These transactions were offset by \$3.6 million in dividends paid on our common stock.

We are subject to minimum risk-based capital limitations as set forth by federal banking regulations at both the consolidated Company level and the Bank level. Under the risk-based capital guidelines, different categories of assets, including certain off-balance sheet items, such as loan commitments in excess of one year and letters of credit, are assigned different risk weights, based generally on the perceived credit risk of the asset. These risk weights are multiplied by corresponding asset balances to determine a risk-weighted asset base. For purposes of the risk-based capital guidelines, total capital is defined as the sum of Tier 1 and Tier 2 capital elements, with Tier 2 capital being limited to 100% of Tier 1 capital. Tier 1 capital includes, with certain restrictions, common shareholders' equity, perpetual preferred stock, and minority interests in consolidated subsidiaries. Tier 2 capital includes, with certain limitations, perpetual preferred stock not included in Tier 1 capital, certain maturing capital instruments, and the allowance for loan and lease losses. As of September 30, 2006, the Company and the Bank are considered Well Capitalized under the regulatory risk based capital guidelines. In order to comply with the regulatory capital constraints, the Company and its Board of Directors constantly monitor the capital level and its anticipated needs based on the Company's growth. The Company has identified sources of additional capital that could be used if needed, and monitors the costs and benefits of these sources, which include both the public and private markets.

Our liquidity management objective is to ensure our ability to satisfy the cash flow requirements of depositors and borrowers and to allow us to sustain our operations. Historically, our primary source of funds has been customer deposits. Scheduled loan repayments are a relatively stable source of funds, while deposit inflows and unscheduled loan prepayments, which are influenced by fluctuations in the general level of interest rates, returns available on other investments, competition, economic conditions, and other factors, are relatively unstable. In addition, the Company has commitments to extend credit under lines of credit and standby letters of credit. The Company has also committed to investing in certain partnerships. Borrowings may be used on a short-term basis to compensate for reductions in other sources of funds (such as deposit inflows at less than projected levels). Borrowings may also be used on a longer-term basis to support expanded lending activities and to match the maturity or repricing intervals of assets. The Company is required under federal banking regulations to maintain sufficient reserves to fund deposit withdrawals, loan commitments, and expenses. We monitor our cash position on a daily basis in order to meet these requirements.

We use various forms of short-term borrowings for cash management and liquidity purposes on a limited basis. These forms of borrowings include federal funds purchased, securities sold under agreements to repurchase, the State of Colorado Treasury's Time Deposit program, and borrowings from the FHLB. The Bank has approved federal funds purchase lines with ten other correspondent banks with an aggregate credit line of \$225.0 million as well as credit lines based on available collateral sources with three firms to transact repurchase agreements. The Bank also has a line of credit from the FHLB that is limited by the amount of eligible collateral available to secure it. Borrowings under the FHLB line are required to be secured by unpledged securities and qualifying loans. At September 30, 2006, we had \$114.4 million in unpledged securities available to collateralize FHLB borrowings and securities sold under agreements to repurchase. We also participate in the U.S. Treasury's Term

Investment Option (TIO) program for Treasury Tax and Loan participants. The TIO program allows us to obtain additional short-term funds at a rate determined through an auction process that is limited by the amount of eligible collateral available to secure it.

At the holding company level, our primary sources of funds are dividends paid from the Bank and fee-based subsidiaries, management fees assessed to the Bank and the fee-based business lines, proceeds from the issuance of common stock, and other capital markets activity. The main use of this liquidity is the quarterly payment of dividends on our common stock, quarterly interest payments on the junior subordinated debentures, payments for mergers and acquisitions activity (including potential earn-out payments), and payments for the salaries and benefits for the employees of the holding company. The approval of the Office of the Comptroller of the Currency is required prior to the declaration of any dividend by the Bank if the total of all dividends declared by the Bank in any calendar year exceeds the total of its net profits for that year combined with the retained net profits for the preceding two years. In addition, the Federal Deposit Insurance Corporation Improvement Act of 1991 provides that the Bank cannot pay a dividend if it will cause the Bank to be undercapitalized. The Company's ability to pay dividends on its common stock depends upon the availability of dividends from the Bank and earnings from its fee-based businesses, and upon the Company's compliance with the capital adequacy guidelines of the Federal Reserve Bank.

The Company expects that cash provided/used by operating activities may fluctuate in future periods as a result of a number of factors, including fluctuations in our operating results and timing of tax and other payments. Management believes that the existing cash, cash equivalent and investments in marketable securities, together with any cash generated from operations will be sufficient to meet normal operating requirements including capital expenditures for the next twelve months. The Company may decide to sell additional equity or debt securities to further enhance our capital position, and the sale of additional equity securities could result in additional dilution to our stockholders. Loan repayments and scheduled investment maturities may provide additional sources of liquidity, if needed.

Net cash provided by operating activities totaled \$19.7 million and \$16.6 million for the nine months ended September 30, 2006 and 2005, respectively. The increase was derived from cash received from both net interest income and non-interest income as well as a reduction in expenditures on other assets, offset by higher operating expenses. Our average interest-earning assets increased by \$228.7 million from September 30, 2005 to September 30, 2006, while our interest-bearing liabilities only increased by \$192.6 million. Our net interest margin decreased slightly to 4.19% for the nine months ended September 30, 2006, from 4.25% as of September 30, 2005. The net increase in our interest-earning assets helped drive our cash receipts from net interest income. Our cash receipts from our fee-based business lines experienced continued increases, primarily due to the M&A transactions closed by GMB and the wealth transfer business of the insurance segment.

Net cash used in investing activities totaled \$188.0 million and \$153.5 million for the nine months ended September 30, 2006 and 2005, respectively. The increase in cash used in investing activities is primarily related to a \$26.9 million increase in net loan originations and a \$28.4 million decrease in cash inflows from investment maturities, offset by a \$17.8 million decrease in investment and BOLI purchases. The Company continues to target an asset mix whereby investments comprise approximately 25% of total assets, which may change based on the Company's collateral needs.

Net cash provided by financing activities totaled \$176.4 million and \$151.3 million for the nine months ended September 30, 2006 and 2005, respectively. The increase in net cash provided by financing activities is primarily attributed to a \$118.0 million net increase in short-term wholesale funding (federal funds purchased, securities sold under agreement to repurchase, and advances from the FHLB). These

items were offset by an \$80.2 million decrease in demand, NOW, money market and savings account inflows as well as a \$14.3 million decrease in inflows from certificates of deposit. Deposit management continues to be an area of focus for the Company as deposits help to provide a source of funding for loans and investments for Company operations. During short-term periods the Company may utilize FHLB advances; fed funds purchased or brokered CDs in an effort to meet certain funding requirements. These sources of funds may come at a higher cost thereby placing pressure on the Company's net interest margin.

Effects of Inflation and Changing Prices

The primary impact of inflation on our operations is increased operating costs. Unlike most retail or manufacturing companies, virtually all of the assets and liabilities of a financial institution such as the Bank are monetary in nature. As a result, the impact of interest rates on a financial institution's performance is generally greater than the impact of inflation. Although interest rates do not necessarily move in the same direction, or to the same extent, as the prices of goods and services, increases in inflation generally have resulted in increased interest rates. Over short periods of time, interest rates may not move in the same direction, or at the same magnitude, as inflation.

Forward Looking Statements

This report contains forward-looking statements that describe CoBiz's future plans, strategies and expectations. All forward-looking statements are based on assumptions and involve risks and uncertainties, many of which are beyond our control and which may cause our actual results, performance or achievements to differ materially from the results, performance or achievements contemplated by the forward-looking statements. Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts. They often include words such as believe, expect, anticipate, intend, plan, estimate or words of similar meaning, or future or conditional verbs such as would, should, could or may. Forward-looking statements speak only as of the date they are made. Such risks and uncertainties include, among other things:

- Competitive pressures among depository and other financial institutions nationally and in our market areas may increase significantly.
- Adverse changes in the economy or business conditions, either nationally or in our market areas, could increase credit-related losses and expenses and/or limit growth.
- Increases in defaults by borrowers and other delinquencies could result in increases in our provision for losses on loans and related expenses.
- Our inability to manage growth effectively, including the successful expansion of our customer support, administrative infrastructure and internal management systems, could adversely affect our results of operations and prospects.
- Fluctuations in interest rates and market prices could reduce our net interest margin and asset valuations and increase our expenses.
- The consequences of continued bank acquisitions and mergers in our market areas, resulting in fewer but much larger and financially stronger competitors, could increase competition for financial services to our detriment.
- Our continued growth will depend in part on our ability to enter new markets successfully and capitalize on other growth opportunities.
- Changes in legislative or regulatory requirements applicable to us and our subsidiaries could increase costs, limit certain operations and adversely affect results of operations.
- Changes in tax requirements, including tax rate changes, new tax laws and revised tax law interpretations may increase our tax expense or adversely affect our customers' businesses.



- Those risks identified under Risk Factors in our annual report on Form 10-K for the year ended December 31, 2005

In light of these risks, uncertainties and assumptions, you should not place undue reliance on any forward-looking statements in this report. We undertake no obligation to publicly update or otherwise revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

As of September 30, 2006, there have been no material changes in the quantitative and qualitative information about market risk provided pursuant to Item 305 of Regulation S-K as presented in our Form 10-K for the year ended December 31, 2005.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and the Company's Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of September 30, 2006 (Evaluation Date) pursuant to Exchange Act Rule 13a-15(e). Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's periodic Securities and Exchange Commission filings.

Disclosure controls and procedures are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control. During the quarter that ended on the Evaluation Date, there were no changes in internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 6. Exhibits

Exhibits and Index of Exhibits.

- 31.1 Rule 13a-14(a)/15d-14(a) Certification of the Chief Executive Officer.
- 31.2 Rule 13a-14(a)/15d-14(a) Certification of the Chief Financial Officer.
- 32.1 Section 1350 Certification of the Chief Executive Officer.
- 32.2 Section 1350 Certification of the Chief Financial Officer.

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SIGNATURES

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In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

COBIZ INC.

Date: November 9, 2006

By */s/ Steven Bangert*
Steven Bangert, Chief Executive Officer and Chairman

Date: November 9, 2006

By */s/ Lyne B. Andrich*
Lyne B. Andrich, Executive Vice President and
Chief Financial Officer

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