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HARRIS PREFERRED CAPITAL CORP

Form 10-Q

May 15, 2003

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2003

COMMISSION FILE NUMBER 1-13805

HARRIS PREFERRED CAPITAL CORPORATION
(Exact name of registrant as specified in its charter)

MARYLAND
(State or other jurisdiction
of incorporation or organization)
111 WEST MONROE STREET, CHICAGO, ILLINOIS
(Address of principal executive offices)

36-4183096
(I.R.S. Employer Identification No.)
60603
(Zip Code)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE:
(312) 461-2121

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 an accelerated filer (as defined in rule 12b-2 of the Act).

Yes No

The number of shares of Common Stock, \$1.00 par value, outstanding on May 14, 2003 was 1,000.

HARRIS PREFERRED CAPITAL CORPORATION

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Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations.....	6
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	The above financial statements, financial review and controls and procedures discussion, included in the Corporation's 2003 First Quarter Report, are filed as Exhibit A and incorporated herein by reference.	
Part II	OTHER INFORMATION	
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	(a) Exhibits	
	99.1 Certification pursuant to 18 U.S.C. Section 1350, As adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	
	(b) Reports on Form 8-K	
	None	
Signatures.....		17
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HARRIS PREFERRED CAPITAL CORPORATION

BALANCE SHEETS
(UNAUDITED)

	MARCH 31, 2003	DECEMBER 31, 2002	MARCH 31, 2001
	-----	-----	-----
	(IN THOUSANDS, EXCEPT SHARE DATA)		
ASSETS			
Cash on deposit with Harris Trust and Savings Bank.....	\$ 246	\$ 728	\$ 1,000
Securities purchased from Harris Trust and Savings Bank under agreement to resell.....	22,000	20,000	14,000
Notes receivable from Harris Trust and Savings Bank.....	27,230	31,078	48,000
Securities available-for-sale:			
Mortgage-backed.....	325,834	365,383	301,000
U.S. Treasury.....	149,991	79,976	119,000
Securing mortgage collections due from Harris Trust and Savings Bank.....	991	2,930	1,000
Other assets.....	1,587	1,947	1,000

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TOTAL ASSETS.....	----- \$527,879 =====	----- \$502,042 =====	----- \$488 =====
LIABILITIES AND STOCKHOLDERS' EQUITY			
Broker payable -- unsettled security purchase.....	\$ 25,066	\$ --	\$
Accrued expenses.....	83	96	
TOTAL LIABILITIES.....	----- 25,149 =====	----- 96 =====	----- =====
Commitments and contingencies.....	--	--	
STOCKHOLDERS' EQUITY			
7 3/8% Noncumulative Exchangeable Preferred Stock, Series A (\$1 par value); liquidation value of \$250,000; 20,000,000 shares authorized, 10,000,000 shares issued and outstanding.....	250,000	250,000	250
Common stock (\$1 par value); 1,000 shares authorized, issued and outstanding.....	1	1	
Additional paid-in capital.....	240,733	240,733	240
Earnings in excess of distributions.....	3,867	850	1
Accumulated other comprehensive income (loss) -- unrealized gains/(losses) on available-for-sale securities.....	8,129	10,362	(4
TOTAL STOCKHOLDERS' EQUITY.....	----- 502,730 -----	----- 501,946 -----	----- 487 -----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY.....	----- \$527,879 =====	----- \$502,042 =====	----- \$488 =====

The accompanying notes are an integral part of these financial statements.

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HARRIS PREFERRED CAPITAL CORPORATION

STATEMENTS OF INCOME
AND COMPREHENSIVE INCOME
(UNAUDITED)

	QUARTER ENDED MARCH 31	
	2003	2002
	-----	-----
(IN THOUSANDS, EXCEPT PER SHARE DATA)		
INTEREST INCOME:		
Securities purchased from Harris Trust and Savings Bank under agreement to resell.....	\$ 247	\$ 320
Notes receivable from Harris Trust and Savings Bank.....	472	845
Securities available-for-sale:		
Mortgage-backed.....	4,526	4,683
U.S. Treasury.....	48	97
Total interest income.....	----- 5,293	----- 5,945
NON-INTEREST INCOME:		
Gain on sale of securities.....	2,463	--
OPERATING EXPENSES:		

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Loan servicing fees paid to Harris Trust and Savings Bank.....	22	41
Advisory fees paid to Harris Trust and Savings Bank.....	10	8
General and administrative.....	98	77
	-----	-----
Total operating expenses.....	130	126
	-----	-----
Net income.....	7,626	5,819
Preferred dividends.....	4,609	4,609
	-----	-----
NET INCOME AVAILABLE TO COMMON STOCKHOLDER.....	\$ 3,017	\$ 1,210
	=====	=====
Basic and diluted earnings per common share.....	\$3,017.00	\$1,210.00
	=====	=====
Net income.....	\$ 7,626	\$ 5,819
Other comprehensive loss -- unrealized losses on available-for-sale securities.....	(2,233)	(2,518)
	-----	-----
Comprehensive income.....	\$ 5,393	\$ 3,301
	=====	=====

The accompanying notes are an integral part of these financial statements.

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HARRIS PREFERRED CAPITAL CORPORATION
STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(UNAUDITED)

	QUARTER ENDED MARCH 31	
	2003	2002
	-----	-----
	(IN THOUSANDS, EXCEPT PER SHARE DATA)	
BALANCE AT JANUARY 1.....	\$501,946	\$489,242
Net income.....	7,626	5,819
Other comprehensive loss.....	(2,233)	(2,518)
Dividends (preferred stock \$0.4609 per share).....	(4,609)	(4,609)
	-----	-----
BALANCE AT MARCH 31.....	\$502,730	\$487,934
	=====	=====

The accompanying notes are an integral part of these financial statements.

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HARRIS PREFERRED CAPITAL CORPORATION
STATEMENTS OF CASH FLOWS
(UNAUDITED)

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	QUARTER ENDED MARCH 31	
	2003	2002
	(IN THOUSANDS)	
OPERATING ACTIVITIES:		
Net Income.....	\$ 7,626	\$ 5,819
Adjustments to reconcile net income to net cash provided by operating activities:		
Gain on sale of securities.....	(2,463)	--
Net decrease in other assets.....	360	118
Net decrease in accrued expenses.....	(13)	(5)
	-----	-----
Net cash provided by operating activities.....	5,510	5,932
	-----	-----
INVESTING ACTIVITIES:		
Net (decrease) increase in securities purchased from Harris Trust and Savings Bank under agreement to resell.....	(2,000)	7,000
Repayments of notes receivable from Harris Trust and Savings Bank.....	3,848	7,590
Decrease in securing mortgage collections due from Harris Trust and Savings Bank.....	1,939	3,658
Purchases of securities available-for-sale.....	(149,929)	(119,909)
Proceeds from maturities and sales of securities available-for-sale.....	144,759	100,049
	-----	-----
Net cash used in investing activities.....	(1,383)	(1,612)
	-----	-----
FINANCING ACTIVITIES:		
Cash dividends paid on preferred stock.....	(4,609)	(4,609)
	-----	-----
Net decrease in cash on deposit with Harris Trust and Savings Bank.....	(482)	(289)
Cash on deposit with Harris Trust and Savings Bank at beginning of period.....	728	506
	-----	-----
Cash on deposit with Harris Trust and Savings Bank at end of period.....	\$ 246	\$ 217
	=====	=====
NON-CASH TRANSACTION:		
Unsettled security purchase.....	\$ 25,066	\$ --
	=====	=====

The accompanying notes are an integral part of these financial statements.

HARRIS PREFERRED CAPITAL CORPORATION
NOTES TO FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

Harris Preferred Capital Corporation (the "Company") is a Maryland corporation whose principal business objective is to acquire, hold, finance and manage qualifying real estate investment trust ("REIT") assets (the "Mortgage Assets"), consisting of a limited recourse note or notes (the "Notes") issued by Harris Trust and Savings Bank (the "Bank") secured by real estate mortgage

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assets (the "Securing Mortgage Loans") and other obligations secured by real property, as well as certain other qualifying REIT assets. The Company holds its assets through a Maryland real estate investment trust subsidiary, Harris Preferred Capital Trust. Harris Capital Holdings, Inc., a wholly-owned subsidiary of the Bank, owns 100% of the Company's common stock.

The accompanying financial statements have been prepared by management from the books and records of the Company, without audit by independent certified public accountants. These statements reflect all adjustments and disclosures which are, in the opinion of management, necessary for a fair statement of the results for the interim periods presented and should be read in conjunction with the notes to financial statements included in the Company's 2002 Form 10-K. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission.

2. COMMITMENTS AND CONTINGENCIES

Legal proceedings in which the Company is a defendant may arise in the normal course of business. There is no pending litigation against the Company.

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

FORWARD-LOOKING INFORMATION

The statements contained in this Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including statements regarding the Company's expectation, intentions, beliefs or strategies regarding the future. Forward-looking statements include the Company's statements regarding tax treatment as a real estate investment trust, liquidity, provision for loan losses, capital resources and investment activities. In addition, in those and other portions of this document, the words "anticipate," "believe," "estimate," "expect," "intend" and other similar expressions, as they relate to the Company or the Company's management, are intended to identify forward-looking statements. Such statements reflect the current views of the Company with respect to future events and are subject to certain risks, uncertainties and assumptions. It is important to note that the Company's actual results could differ materially from those described herein as anticipated, believed, estimated or expected. Among the factors that could cause the results to differ materially are the risks discussed in the "Risk Factors" section included in the Company's Registration Statement on Form S-11 (File No. 333-40257), with respect to the Preferred Shares declared effective by the Securities and Exchange Commission on February 5, 1998. The Company assumes no obligation to update any such forward-looking statement.

RESULTS OF OPERATIONS

FIRST QUARTER 2003 COMPARED WITH FIRST QUARTER 2002

The Company's net income for the first quarter of 2003 was \$7.6 million. This represented a \$1.8 million or 31% increase from first quarter 2002 earnings of \$5.8 million. Earnings increased primarily because of a \$2.5 million gain on sale of securities in 2003 compared to no gains in 2002, partially offset by a decline in interest income on investments.

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First quarter 2003 interest income on the Notes totaled \$472 thousand and yielded 6.4% on \$29.7 million of average principal outstanding for the quarter compared to \$845 thousand and a 6.4% yield on \$52.9 million average principal outstanding for first quarter 2002. The decrease in income was attributable to a reduction in the Notes balance because of principal paydowns by customers in the underlying Securing Mortgage Loans. The average outstanding balance of the Securing Mortgage Loans for first quarter 2003 and 2002 was \$36 million and \$65 million, respectively. Interest income on securities available-for-sale for the current quarter was \$4.6 million resulting in a yield of 5.0% on an average balance of \$368 million, compared to \$4.8 million with a yield of 5.7% on an average balance of \$335 million for the same period a year ago. The decrease in interest income is primarily attributable to the reduction in yield. As securities mature or are sold, proceeds have been invested in lower yielding securities because market interest rates have generally been declining.

There were no Company borrowings during first quarter 2003 or 2002.

First quarter 2003 operating expenses totaled \$130 thousand, an increase of \$4 thousand or 3% from the first quarter of 2002. Loan servicing expenses totaled \$22 thousand, a decrease of \$19 thousand or 46% from a year ago. This decrease is attributable to the reduction in the principal balance of the Notes, thereby reducing servicing fees payable to the Bank. Advisory fees for the first quarter 2003 were \$10 thousand compared to \$8 thousand a year earlier. General and administrative expenses totaled \$98 thousand, an increase of \$21 thousand or 27% over the same period in 2002, as a result of additional corporate governance costs.

At March 31, 2003 and 2002, there were no Securing Mortgage Loans on nonaccrual status.

The Company does not currently maintain an allowance for loan losses due to the over-collateralization of the Notes represented by the Securing Mortgage Loans.

LIQUIDITY RISK MANAGEMENT

The objective of liquidity management is to ensure the availability of sufficient cash flows to meet all of the Company's financial commitments. In managing liquidity, the Company takes into account various legal limitations placed on a REIT.

The Company's principal asset management requirements are to maintain the current earning asset portfolio size through the acquisition of additional Notes or other qualifying assets in order to pay dividends to its stockholders after satisfying obligations to creditors. The acquisition of additional Notes or other qualifying assets is funded with the proceeds obtained as a result of repayment of principal balances of individual Securing Mortgage Loans or maturities or sales of securities. The payment of dividends on the Preferred Shares is made from legally available funds, arising from operating activities of the Company. The Company's cash flows from operating activities principally consist of the collection of interest on the Notes, mortgage-backed securities and other earning assets. The Company does not have and does not anticipate having any material capital expenditures.

In order to remain qualified as a REIT, the Company must distribute annually at least 90% of its adjusted REIT ordinary taxable income, as provided for under the Internal Revenue Code, to its common and preferred stockholders. The Company currently expects to distribute dividends annually equal to 90% or more of its adjusted REIT ordinary taxable income.

The Company anticipates that cash and cash equivalents on hand and the cash flow from the Notes and mortgage-backed securities will provide adequate

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liquidity for its operating, investing and financing needs.

As presented in the accompanying Statements of Cash Flows, the primary sources of funds in addition to \$5.5 million provided from operations during the three months ended March 31, 2003 were \$3.8 million provided by principal repayments on the Notes and \$144.8 million from the maturities and sales of securities available-for-sale. In the prior period ended March 31, 2002, the primary sources of funds other than

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HARRIS PREFERRED CAPITAL CORPORATION NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

\$5.9 million from operations were \$7.6 million provided by principal repayments on the Notes and \$100.0 million from the maturities and sales of securities available-for-sale. The primary uses of funds for the three months ended March 31, 2003 were \$149.9 million for purchases of securities available-for-sale and \$4.6 million in preferred stock dividends paid. For the prior year's quarter ended March 31, 2002, the primary uses of funds were \$119.9 million for purchases of securities available-for-sale and \$4.6 million in preferred stock dividends paid.

MARKET RISK MANAGEMENT

The Company's market risk is composed primarily of interest rate risk. There have been no material changes in market risk or the manner in which the Company manages market risk since December 31, 2002.

OTHER MATTERS

As of March 31, 2003, the Company believes that it is in full compliance with the REIT tax rules, and expects to qualify as a REIT under the provisions of the Code. The Company expects to meet all REIT requirements regarding the ownership of its stock and anticipates meeting the annual distribution requirements.

FINANCIAL STATEMENTS OF HARRIS TRUST AND SAVINGS BANK

The following unaudited financial information for the Bank is included because the Company's preferred shares are automatically exchangeable for a new series of preferred stock of the Bank upon the occurrence of certain events.

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HARRIS TRUST AND SAVINGS BANK AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF CONDITION (UNAUDITED)

	MARCH 31 2003	DECEMBER 31 2002
	-----	-----
	(IN THOUSANDS EXCEPT SHA	
ASSETS		
Cash and demand balances due from banks.....	\$ 1,244,415	\$ 1,057,254
Money market assets:		
Interest-bearing deposits at banks.....	321,090	417,206
Federal funds sold and securities purchased under agreement to resell.....	467,875	237,950

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Securities available-for-sale (including \$4.39 billion, \$4.39 billion and \$2.61 billion of securities pledged as collateral for repurchase at March 31, 2003, December 31, 2002 and March 31, 2002, respectively).....	6,183,136	5,781,360
Trading account assets.....	34,541	42,423
Loans.....	9,767,905	9,607,887
Allowance for possible loan losses.....	(208,281)	(206,999)
	-----	-----
Net loans.....	9,559,624	9,400,888
Premises and equipment.....	298,711	298,414
Customers' liability on acceptances.....	23,125	16,168
Bank-owned insurance.....	1,005,261	994,185
Loans held for sale.....	197,653	149,311
Goodwill and other valuation intangibles.....	184,372	187,317
Other assets.....	523,914	444,542
	-----	-----
TOTAL ASSETS.....	\$20,043,717	\$19,027,018
	=====	=====
LIABILITIES		
Deposits in domestic offices -- noninterest bearing.....	\$ 2,053,114	\$ 2,085,400
-- interest-bearing.....	8,519,578	7,736,930
Deposits in foreign offices -- noninterest bearing.....	39,021	31,383
-- interest-bearing.....	906,958	1,184,571
	-----	-----
Total deposits.....	11,518,671	11,038,284
Federal funds purchased and securities sold under agreement to repurchase.....	5,250,145	5,060,784
Short-term borrowings.....	200,649	300,694
Short-term notes -- senior.....	350,000	200,000
Acceptances outstanding.....	23,125	16,168
Accrued interest, taxes and other expenses.....	141,359	153,148
Other liabilities.....	495,790	200,286
Minority interest -- preferred stock of subsidiary.....	250,000	250,000
Preferred stock issued to Harris Bankcorp, Inc.	5,000	5,000
Long-term notes -- subordinated.....	225,000	225,000
	-----	-----
TOTAL LIABILITIES.....	18,459,739	17,449,364
	-----	-----
STOCKHOLDER'S EQUITY		
Common stock (\$10 par value); 10,000,000 shares authorized, issued and outstanding.....	100,000	100,000
Surplus.....	629,381	626,640
Retained earnings.....	816,552	803,249
Accumulated other comprehensive income (loss).....	38,045	47,765
	-----	-----
TOTAL STOCKHOLDER'S EQUITY.....	1,583,978	1,577,654
	-----	-----
TOTAL LIABILITIES AND STOCKHOLDER'S EQUITY.....	\$20,043,717	\$19,027,018
	=====	=====

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

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	QUARTER ENDED MARCH 31	
	2003	2002
	-----	-----
	(IN THOUSANDS EXCEPT SHARE DATA)	
INTEREST INCOME		
Loans, including fees.....	\$117,492	\$131,020
Money market assets:		
Deposits at banks.....	993	181
Federal funds sold and securities purchased under agreement to resell.....	695	1,817
Trading account.....	453	509
Securities available-for-sale:		
U.S. Treasury and Federal agency.....	42,509	58,321
State and municipal.....	5	14
Other.....	1,121	549
	-----	-----
Total interest income.....	163,268	192,411
	-----	-----
INTEREST EXPENSE		
Deposits.....	30,319	42,861
Short-term borrowings.....	14,220	17,649
Senior notes.....	895	6,077
Minority interest-dividends on preferred stock of subsidiary.....	4,609	4,609
Long-term notes.....	2,677	2,852
	-----	-----
Total interest expense.....	52,720	74,048
	-----	-----
NET INTEREST INCOME.....	110,548	118,363
Provision for loan losses.....	17,618	28,557
	-----	-----
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES.....	92,930	89,806
	-----	-----
NONINTEREST INCOME		
Trust and investment management fees.....	19,738	19,591
Money market and bond trading.....	3,125	1,684
Foreign exchange.....	976	3,148
Service fees and charges.....	27,724	30,082
Securities gains.....	2,463	15,374
Bank-owned insurance.....	10,796	12,814
Foreign fees.....	6,218	6,025
Other.....	50,268	41,008
	-----	-----
Total noninterest income.....	121,308	129,726
	-----	-----
NONINTEREST EXPENSES		
Salaries and other compensation.....	78,768	76,765
Pension, profit sharing and other employee benefits.....	18,123	15,147
Net occupancy.....	9,808	9,343
Equipment.....	13,069	13,714
Marketing.....	7,215	7,338
Communication and delivery.....	5,598	5,567
Expert services.....	6,214	6,270
Contract programming.....	6,343	7,025
Other.....	18,913	14,595
	-----	-----

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	164,051	155,764
Goodwill and other valuation intangibles.....	4,150	3,823
	-----	-----
Total noninterest expenses.....	168,201	159,587
	-----	-----
Income before income taxes.....	46,037	59,945
Applicable income taxes.....	12,615	16,445
	-----	-----
NET INCOME.....	\$ 33,422	\$ 43,500
	=====	=====
EARNINGS PER COMMON SHARE (based on 10,000,000 average shares outstanding)		
Net Income.....	\$ 3.34	\$ 4.35
	=====	=====

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

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HARRIS TRUST AND SAVINGS BANK AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

	QUARTER ENDED MARCH 31	
	2003	2002
	----	----
	(IN THOUSANDS)	
NET INCOME.....	\$33,422	\$ 43,500
OTHER COMPREHENSIVE INCOME:		
Unrealized losses on available-for-sale securities:		
Unrealized holding losses arising during the period, net of tax benefit of \$5,453 in 2003 and \$8,761 in 2002.....	(8,216)	(12,954)
Less reclassification adjustment for realized gains included in income statement, net of tax expense of \$958 in 2003 and \$5,980 in 2002.....	(1,505)	(9,394)
	-----	-----
Other comprehensive loss.....	(9,721)	(22,348)
	-----	-----
COMPREHENSIVE INCOME.....	\$23,701	\$ 21,152
	=====	=====

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

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HARRIS TRUST AND SAVINGS BANK AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDER'S EQUITY
(UNAUDITED)

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	2003	2002
	----	----
	(IN THOUSANDS)	
BALANCE AT JANUARY 1.....	\$1,577,654	\$1,560,677
Net income.....	33,422	43,500
Contributions to capital.....	2,741	1,707
Dividends -- preferred stock.....	(119)	(143)
Dividends -- common stock.....	(20,000)	--
Other comprehensive loss.....	(9,720)	(22,349)
	-----	-----
BALANCE AT MARCH 31.....	\$1,583,978	\$1,583,392
	=====	=====

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

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HARRIS TRUST AND SAVINGS BANK AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	QUARTER ENDED MARCH 31	
	2003	2002
	----	----
	(IN THOUSANDS)	
OPERATING ACTIVITIES:		
Net Income.....	\$ 33,422	\$ 43,500
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses.....	17,617	28,557
Depreciation and amortization, including intangibles.....	16,477	14,485
Deferred tax benefit.....	(1,411)	(500)
Gain on sales of securities.....	(2,463)	(15,374)
Increase in bank-owned insurance.....	(11,076)	(12,104)
Trading account net cash sales.....	38,689	71,101
Net (increase) decrease in interest receivable.....	(1,057)	5,107
Net increase in interest payable.....	4,722	6,397
Net increase in loans held for sale.....	(48,342)	(23,723)
Other, net.....	10,979	(6,778)
	-----	-----
Net cash provided by operating activities.....	57,557	110,668
	-----	-----
INVESTING ACTIVITIES:		
Net decrease (increase) in interest-bearing deposits at banks.....	96,116	(6,266)
Net increase in Federal funds sold and securities purchased under agreement to resell.....	(229,925)	(389,400)
Proceeds from sales of securities available-for-sale.....	44,761	339,285
Proceeds from maturities of securities		

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available-for-sale.....	1,180,838	1,355,439
Purchases of securities available-for-sale.....	(1,466,830)	(1,020,785)
Net (increase) decrease in loans.....	(182,435)	152,455
Purchases of premises and equipment.....	(12,624)	(12,105)
	-----	-----
Net cash (used) provided by investing activities.....	(570,099)	418,623
	-----	-----
FINANCING ACTIVITIES:		
Net increase (decrease) in deposits.....	480,387	(164,177)
Net increase (decrease) in Federal funds purchased and securities sold under agreement to repurchase.....	189,361	(631,013)
Net decrease in other short-term borrowings.....	(100,045)	(190,894)
Proceeds from issuance of senior notes.....	750,000	--
Repayment of senior notes.....	(600,000)	--
Cash dividends paid on common stock.....	(20,000)	--
	-----	-----
Net cash provided (used) by financing activities.....	699,703	(986,084)
	-----	-----
NET INCREASE IN CASH AND DEMAND BALANCES DUE FROM BANKS.....		
	187,161	(456,793)
CASH AND DEMAND BALANCES DUE FROM BANKS AT JANUARY 1...	1,057,254	1,203,945
	-----	-----
CASH AND DEMAND BALANCES DUE FROM BANKS AT MARCH 31....	\$ 1,244,415	\$ 747,152
	=====	=====

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

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HARRIS TRUST AND SAVINGS BANK AND SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

Harris Trust and Savings Bank (the "Bank") is a wholly-owned subsidiary of Harris Bankcorp, Inc. ("Bankcorp"), a wholly-owned subsidiary of Bankmont Financial Corp. (a wholly-owned subsidiary of Bank of Montreal). The consolidated financial statements of the Bank include the accounts of the Bank and its wholly-owned subsidiaries. Significant intercompany accounts and transactions have been eliminated. Certain reclassifications were made to conform prior year's financial statements to the current year's presentation.

The consolidated financial statements have been prepared by management from the books and records of the Bank, without audit by independent certified public accountants. However, these statements reflect all adjustments and disclosures which are, in the opinion of management, necessary for a fair presentation of the results for the interim periods presented.

Because the results of operations are so closely related to and responsive to changes in economic conditions, the results for any interim period are not necessarily indicative of the results that can be expected for the entire year.

2. LEGAL PROCEEDINGS

The Bank and certain of its subsidiaries are defendants in various legal proceedings arising in the normal course of business. In the opinion of management, based on the advice of legal counsel, the ultimate resolution of these matters will not have a material adverse effect on the Bank's consolidated

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financial position.

3. CASH FLOWS

For purposes of the Bank's Consolidated Statements of Cash Flows, cash and cash equivalents is defined to include cash and demand balances due from banks. Cash interest payments (net of amounts capitalized) for the three months ended March 31 totaled \$48.0 million and \$67.7 million in 2003 and 2002, respectively. Cash income tax payments totaled \$0.1 million in both the three months ended March 31, 2003 and 2002.

4. GOODWILL AND OTHER INTANGIBLE ASSETS

The Bank adopted Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets," on January 1, 2002. Under this standard, goodwill and other intangible assets that have indefinite useful lives are not subject to amortization while intangible assets with finite lives are amortized. Goodwill is periodically assessed for impairment, at least annually. Upon adoption of SFAS No. 142, the Bank had no goodwill.

The Bank adopted SFAS No. 147, "Acquisitions of Certain Financial Institutions--an amendment of FASB Statements No. 72 and 144 and FASB Interpretation No. 9," on October 1, 2002. Under this standard, most acquisitions of financial institutions are removed from the scope of SFAS No. 72 and Interpretation No. 9 and are accounted for in accordance with SFAS No. 141, "Business Combinations," and SFAS No. 142. As such, unidentifiable intangible assets recognized and amortized in accordance with SFAS No. 72, "Accounting for Certain Acquisitions of Banking or Thrift Institutions," represent goodwill that will be accounted for under SFAS No. 142. At adoption date, the Bank had an unidentifiable intangible asset that, in accordance with SFAS No. 72, was excluded from the scope of SFAS No. 142 and continued to be amortized through third quarter 2002. Upon adoption of the Statement, the unidentifiable intangible asset was reclassified to goodwill and no longer amortized starting in fourth quarter 2002. Under the transitional requirements of the Statement, the first three quarters of 2002 were restated to reflect the reversal of previously amortized goodwill in those quarters. The earnings impact for each of these three quarters was \$2.35 million pretax (\$1.4 million after tax).

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HARRIS TRUST AND SAVINGS BANK AND SUBSIDIARIES

NOTES TO THE FINANCIAL STATEMENTS -- (CONTINUED)

The Bank's goodwill was subject to the annual impairment test in the fourth quarter of 2002. The fair value of the reporting unit was estimated using a valuation technique based on multiples of book value. The test did not identify potential impairment and no impairment loss was recognized in 2002.

The carrying value of the Bank's goodwill as of March 31, 2003 was \$89.3 million.

As of March 31, 2003, the gross carrying amount and accumulated amortization of the Bank's amortizable intangible assets were \$205.1 million and \$110.0 million, respectively.

Total amortization expense for the Bank's intangible assets was \$4.1 million for the quarter ended March 31, 2003.

Estimated intangible asset amortization expense for the years ending December 31, 2004, 2005, 2006, 2007 and 2008 is \$16.4 million, \$16.5 million, \$16.7 million, \$16.9 million and \$17.1 million, respectively.

HARRIS TRUST AND SAVINGS BANK AND SUBSIDIARIES

FINANCIAL REVIEW

FIRST QUARTER 2003 COMPARED WITH FIRST QUARTER 2002

SUMMARY

The Bank had first quarter 2003 net income of \$33.4 million, a decrease of \$10.1 million or 23 percent from first quarter 2002.

Cash ROE was 10.69 percent in the current quarter and 13.30 percent in first quarter 2002. Excluding unrealized gains and losses on the securities portfolio recorded directly to equity, cash ROE was 11.03 percent for the current year's first quarter, compared to 13.57 percent a year ago. The income from continued strong growth in consumer, mortgage, and small business loans and retail deposits and from a reduced loan loss provision was more than offset by lower net interest income and noninterest income, primarily gains from sales of securities.

First quarter net interest income on a fully taxable equivalent basis was \$113.6 million, down \$7.3 million or 6 percent from \$120.9 million in 2002's first quarter. Average earning assets decreased 1 percent to \$15.85 billion from \$15.97 billion in 2002. Average loans decreased \$383 million which was offset by an increase in the investment portfolio of \$280 million. Net interest margin decreased to 2.90 percent from 3.06 percent in the same quarter last year.

The first quarter 2003 provision for loan losses of \$17.6 million was down from \$28.6 million in the first quarter of 2002. Net charge-offs were \$16.3 million compared to \$36.2 million in the prior year's quarter. Most of the increase resulted from lower commercial loan write offs.

First quarter 2003 noninterest income of \$87.2 million decreased \$15.1 million from the same quarter last year. Most of the decline was the result of a \$12.9 million reduction in net gains from securities sales compared to a year ago quarter. Bond trading profits and syndication fees increased from first quarter 2002.

First quarter 2003 noninterest expenses of \$134.1 million decreased \$2.0 million or 1 percent from the year-ago quarter.

Nonperforming assets at March 31, 2003 were \$175 million or 1.79 percent of total loans, compared to \$172 million or 1.79 percent at December 31, 2002, and \$206 million or 2.10 percent a year ago. At March 31, 2003, the allowance for possible loan losses was \$208 million, equal to 2.13 percent of loans outstanding, compared to \$220 million or 2.25 percent at the end of first quarter 2002. As a result, the ratio of the allowance for possible loan losses to nonperforming assets was 107 percent at March 31, 2002 compared to 119 percent at March 31, 2003.

At March 31, 2003, Tier 1 capital of the Bank amounted to \$1.59 billion, down from \$1.65 billion one year earlier. The regulatory leverage capital ratio was 8.70 percent for the first quarter of 2003 compared to 8.91 percent in the same quarter of 2002. The Bank's capital ratio exceeds the prescribed regulatory minimum for banks. The Bank's March 31, 2003 Tier 1 and total risk-based capital ratios were 9.92 percent and 12.12 percent compared to respective ratios of 10.40 percent and 12.83 percent at March 31, 2002.

ITEM 4. CONTROLS AND PROCEDURES

Within 90 days prior to the filing of this report, Paul R. Skubic, the Chairman of the Board, Chief Executive Officer and President of the Company, and Pamela C. Piarowski, the Chief Financial Officer of the Company, evaluated the effectiveness of the disclosure controls and procedures of the Company and concluded that these disclosure controls and procedures are effective to ensure that material information required to be included in this Report has been made known to them in a timely fashion. There were no significant changes in the Company's internal controls or in other factors that could significantly affect these internal controls subsequent to the date of their evaluation, including any corrective action with regard to significant deficiencies and material weaknesses.

PART II. OTHER INFORMATION

ITEMS 1, 2, 3, 4 AND 5 ARE BEING OMITTED FROM THIS REPORT BECAUSE SUCH ITEMS ARE NOT APPLICABLE TO THE REPORTING PERIOD.

ITEM 6. (a) EXHIBITS

99.1 CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

(b) Reports on Form 8-K: None

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, Harris Preferred Capital Corporation has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized on the 14th day of May 2003.

/s/ PAUL R. SKUBIC

Paul R. Skubic
Chairman of the Board and President

/s/ PAMELA C. PIAROWSKI

Pamela C. Piarowski
Chief Financial Officer

CERTIFICATIONS

I, Paul R. Skubic, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Harris Preferred Capital Corporation;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

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3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of Harris Preferred Capital Corporation as of, and for, the periods presented in this quarterly report;

4. Harris Preferred Capital Corporation's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for Harris Preferred Capital Corporation and we have:

a) designed such disclosure controls and procedures to ensure that material information relating to Harris Preferred Capital Corporation, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of Harris Preferred Capital Corporation's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. Harris Preferred Capital Corporation's other certifying officer and I have disclosed, based on our most recent evaluation, to Harris Preferred Capital Corporation's auditors and the audit committee of Harris Preferred Capital Corporation's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect Harris Preferred Capital Corporation's ability to record, process, summarize and report financial data and have identified for Harris Preferred Capital Corporation's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in Harris Preferred Capital Corporation's internal controls; and

6. Harris Preferred Capital Corporation's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

/s/ PAUL R. SKUBIC

Paul R. Skubic
Chairman of the Board and President

Date: 5/14/03

A signed original of this written statement required by Section 906 has been provided to Harris Preferred Capital Corporation and will be retained by Harris Preferred Capital Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

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CERTIFICATIONS

I, Pamela C. Piarowski, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Harris Preferred Capital Corporation;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of Harris Preferred Capital Corporation as of, and for, the periods presented in this quarterly report;

4. Harris Preferred Capital Corporation's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for Harris Preferred Capital Corporation and we have:

a) designed such disclosure controls and procedures to ensure that material information relating to Harris Preferred Capital Corporation, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of Harris Preferred Capital Corporation's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. Harris Preferred Capital Corporation's other certifying officer and I have disclosed, based on our most recent evaluation, to Harris Preferred Capital Corporation's auditors and the audit committee of Harris Preferred Capital Corporation's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect Harris Preferred Capital Corporation's ability to record, process, summarize and report financial data and have identified for Harris Preferred Capital Corporation's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in Harris Preferred Capital Corporation's internal controls; and

6. Harris Preferred Capital Corporation's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and

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material weaknesses.

/s/ PAMELA C. PIAROWSKI

Pamela C. Piarowski
Chief Financial Officer

Date: 5/14/03

A signed original of this written statement required by Section 906 has been provided to Harris Preferred Capital Corporation and will be retained by Harris Preferred Capital Corporation and furnished to the Securities and Exchange Commission or its staff upon request.