

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

METRIS COMPANIES INC  
Form 10-Q  
August 14, 2001

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
-----

FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended June 30, 2001

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001-12351

METRIS COMPANIES INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State of Incorporation)

41-1849591  
(I.R.S. Employer Identification No.)

10900 Wayzata Boulevard, Minnetonka, Minnesota 55305-1534  
(Address of principal executive offices)

(952) 525-5020  
(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   
-----

As of July 31, 2001, 64,038,903 shares of the registrant's common stock, par value \$.01 per share, were outstanding.

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

METRIS COMPANIES INC.

FORM 10-Q

TABLE OF CONTENTS

June 30, 2001

	Page
	----
PART I.	FINANCIAL INFORMATION
Item 1.	Consolidated Financial Statements (unaudited):
	Consolidated Balance Sheets.....3
	Consolidated Statements of Income.....4
	Consolidated Statements of Changes in
	Stockholders' Equity.....6
	Consolidated Statements of Cash Flows.....7
	Notes to Consolidated Financial Statements.....8
Item 2.	Management's Discussion and Analysis of
	Financial Condition and Results of
	Operations.....22
Item 3.	Quantitative and Qualitative Disclosures
	About Market Risk.....34
PART II.	OTHER INFORMATION
Item 1.	Legal Proceedings.....35
Item 2.	Changes in Securities.....35
Item 3.	Defaults Upon Senior Securities.....35
Item 4.	Submission of Matters to a Vote of Security Holders.....35
Item 5.	Other Information.....36
Item 6.	Exhibits and Reports on Form 8-K.....36
	Signatures.....38

Part I. Financial Information

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

METRIS COMPANIES INC. AND SUBSIDIARIES  
Consolidated Balance Sheets

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

(Dollars in thousands, except per-share data) (Unaudited)

	June 30, 2001	Dec
	-----	-----
<b>Assets:</b>		
Cash and due from banks .....	\$ 101,661	\$
Federal funds sold .....	494,425	
Short-term investments .....	89,297	
	-----	-----
Cash and cash equivalents .....	685,383	
	-----	-----
Retained interests in loans securitized .....	1,069,090	2,
Less: Allowance for loan losses .....	568,084	
	-----	-----
Net retained interests in loans securitized .....	501,006	1,
	-----	-----
Credit card loans (net of allowance for loan losses of \$258,057 and \$123,123, respectively).....	2,054,595	1,
Property and equipment, net .....	124,263	
Deferred income taxes .....	107,181	
Purchased portfolio premium .....	80,291	
Other receivables due from credit card securitizations, net .....	169,035	
Other assets .....	234,578	
	-----	-----
Total assets .....	\$ 3,956,332	\$ 3,
	=====	=====
<b>Liabilities:</b>		
Deposits .....	\$ 2,174,945	\$ 2,
Debt .....	356,337	
Accounts payable .....	137,969	
Deferred income .....	211,331	
Accrued expenses and other liabilities .....	68,502	
	-----	-----
Total liabilities .....	2,949,084	2,
	-----	-----
<b>Stockholders' Equity:</b>		
Convertible preferred stock - Series C, par value \$.01 per share; 10,000,000 shares authorized, 1,011,604 and 967,573 shares issued and outstanding, respectively .....	376,822	
Common stock, par value \$.01 per share; 100,000,000 shares authorized, 63,793,584 and 62,242,787 shares issued and outstanding, respectively .....	638	
Paid-in capital .....	224,068	
Unearned compensation .....	(4,779)	
Retained earnings .....	410,499	
	-----	-----
Total stockholders' equity .....	1,007,248	
	-----	-----
Total liabilities and stockholders' equity .....	\$ 3,956,332	\$ 3,
	=====	=====

See accompanying Notes to Consolidated Financial Statements.

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

METRIS COMPANIES INC. AND SUBSIDIARIES  
 Consolidated Statements of Income  
 (Dollars in thousands, except per-share data) (Unaudited)

	Three Months Ended June 30,	
	2001	2000
	-----	-----
Interest Income:		
Credit card loans and retained interests in loans securitized .....	\$ 168,702	\$ 113,
Federal funds sold .....	329	1,
Other .....	3,176	
	-----	-----
Total interest income .....	172,207	115,
Deposit interest expense .....	32,936	18,
Other interest expense .....	11,377	10,
	-----	-----
Total interest expense .....	44,313	28,
	-----	-----
Net Interest Income .....	127,894	86,
Provision for loan losses .....	114,682	98,
	-----	-----
Net Interest Income (Expense) After Provision for Loan Losses.....	13,212	(11,
	-----	-----
Other Operating Income:		
Net securitization and credit card servicing income .....	119,712	120,
Credit card fees, interchange and other credit card income .....	74,837	53,
Enhancement services revenues .....	82,900	63,
	-----	-----
	277,449	238,
	-----	-----
Other Operating Expense:		
Credit card account and other product solicitation and marketing expenses.....	51,481	36,
Employee compensation .....	56,115	42,
Data processing services and communications .....	22,141	20,
Warranty and debt waiver underwriting and claims servicing expense .....	8,250	6,
Credit card fraud losses .....	2,200	2,
Purchased portfolio premium amortization .....	7,418	5,
Other .....	41,325	33,
	-----	-----
	188,930	148,
	-----	-----
Income Before Income Taxes and Cumulative Effect of Accounting Changes.....	101,731	78,
Income taxes .....	38,963	30,
	-----	-----
Income Before Cumulative Effect of Accounting Changes.....	62,768	48,
Cumulative effect of accounting changes (net of income taxes of \$9,000 and		

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

\$2,180, respectively).....	-----	-----
	-----	-----
Net Income .....	62,768	48,
Convertible preferred stock		
dividends-Series C .....	8,593	7,
	-----	-----
Net Income Applicable To Common		
Stockholders.....	\$ 54,175	\$ 40,
	=====	=====

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2001	2000	2001	2000
	----	----	----	----
Earnings per share:				
Basic-income before cumulative				
effect of accounting changes .....	\$ 0.64	\$ 0.55	\$ 1.22	\$ 1.16
Basic-cumulative effect of accounting				
changes .....	--	--	(0.15)	(0.04)
Basic-net income .....	0.64	0.55	1.07	1.12
Diluted-income before cumulative				
effect of accounting changes .....	0.63	0.53	1.20	1.12
Diluted-cumulative effect of accounting				
changes .....	--	--	(0.15)	(0.04)
Diluted-net income .....	0.63	0.53	1.05	1.08
Shares used to compute earnings per share:				
Basic .....	97,633	88,002	97,117	87,564
Diluted .....	99,841	91,568	99,055	91,118

See accompanying Notes to Consolidated Financial Statements.

METRIS COMPANIES INC. AND SUBSIDIARIES  
Consolidated Statements of Changes in Stockholders' Equity  
(In thousands) (Unaudited)

	Number of Shares	Preferred	Common	Paid-in	Une
	Preferred	Stock	Stock	Capital	Comp
	-----	-----	-----	-----	-----
BALANCE AT DECEMBER 31, 1999 .	885	57,919	\$ 329,729	\$ 386	\$ 130,772
Net income .....	--	--	--	--	--

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Cash dividends .....	--	--	--	--	--	--
Preferred dividends in kind - Series C .....	40	--	15,004	--	--	--
June 2000 three-for-two stock split .....	--	--	--	201	(201)	--
Issuance of common stock under employee benefit plans .....	--	2,480	--	17	33,899	--
BALANCE AT JUNE 30, 2000 .....	925	60,399	\$ 344,733	\$ 604	\$ 164,470	\$ --
<hr/>						
BALANCE AT DECEMBER 31, 2000 .	968	62,243	\$ 360,421	\$ 622	\$ 198,077	\$ --
Net income .....	--	--	--	--	--	--
Cash dividends .....	--	--	--	--	--	--
Preferred dividends in kind - Series C .....	44	--	16,401	--	--	--
Issuance of common stock under employee benefit plans .....	--	1,551	--	16	25,991	--
Compensation expense related to restricted stock granted .....	--	--	--	--	--	--
BALANCE AT JUNE 30, 2001 .....	1,012	63,794	\$ 376,822	\$ 638	\$ 224,068	\$ --
<hr/>						

See accompanying Notes to Consolidated Financial Statements.

METRIS COMPANIES INC. AND SUBSIDIARIES  
Consolidated Statements of Cash Flows  
(Dollars in thousands) (Unaudited)

	Six Months Ended June 30,	
	2001	2000
	----	----
Operating Activities:		
Net income .....	\$ 104,314	\$ 98,238
Adjustments to reconcile net income to net cash provided by operating activities:		
Cumulative effect of accounting changes .....	14,499	3,438
Depreciation and amortization .....	47,929	37,137
Change in allowance for loan losses .....	62,166	58,093
Change in value of derivative instruments .....	(2,990)	--
Changes in operating assets and liabilities, net:		
Deferred income taxes .....	39,164	(15,275)
Other receivables due from credit card securitizations .....	(3,522)	54,198
Accounts payable and accrued expenses .....	50,669	26,213
Deferred income .....	(24,176)	44,916
Other .....	(23,143)	(82,039)
Net cash provided by operating activities .....	264,910	224,919
	-----	-----

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Investing Activities:		
Net proceeds (uses) from sales and repayments of securitized loans.....	692,051	(34,075)
Net loans originated .....	(870,122)	(561,449)
Additions to property and equipment .....	(3,990)	(41,168)
	-----	-----
Net cash used in investing activities .....	(182,061)	(636,692)
	-----	-----
Financing Activities:		
Net increase in debt .....	271	444
Net increase in deposits .....	68,746	469,592
Cash dividends paid .....	(1,847)	(1,137)
Increase in common equity .....	13,924	33,916
	-----	-----
Net cash provided by financing activities .....	81,094	502,815
	-----	-----
Net increase in cash and cash equivalents .....	163,943	91,042
Cash and cash equivalents at beginning of period .....	521,440	194,433
	-----	-----
Cash and cash equivalents at end of period .....	\$ 685,383	\$ 285,475
	=====	=====
Supplemental disclosures and cash flow information:		
Cash paid during the period for:		
Interest .....	\$ 86,731	\$ 40,114
Income taxes .....	25,366	70,284
Tax benefit from employee stock option exercises.....	6,651	16,531

See accompanying Notes to Consolidated Financial Statements.

METRIS COMPANIES INC. AND SUBSIDIARIES  
Notes to Consolidated Financial Statements  
(Dollars in thousands, except as noted) (Unaudited)

### NOTE 1 - ORGANIZATION AND BASIS OF PRESENTATION

The consolidated financial statements include the accounts of Metris Companies Inc. ("MCI") and its subsidiaries, including Direct Merchants Credit Card Bank, N.A. ("Direct Merchants Bank"), which may be referred to as "we," "us," "our" and the "Company." The Company is an information-based direct marketer of consumer credit products and enhancement services primarily to moderate-income consumers.

All significant intercompany balances and transactions have been eliminated in consolidation. Certain prior-year amounts have been reclassified to conform with the current year's presentation.

### Interim Financial Statements

We have prepared the unaudited interim consolidated financial statements and related unaudited financial information in the footnotes in accordance with accounting principles generally accepted in the United States of America and the rules and regulations of the Securities and Exchange Commission ("SEC") for interim financial statements. These interim financial statements reflect all adjustments consisting of normal recurring accruals which, in the opinion of management, are necessary to present fairly our consolidated financial position and the results of our operations and our cash flows for the interim periods.

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

You should read these consolidated financial statements in conjunction with the financial statements and the notes thereto contained in our annual report on Form 10-K for the fiscal year ended December 31, 2000. The nature of our business is such that the results of any interim period may not be indicative of the results to be expected for the entire year.

### Pervasiveness of Estimates

We have prepared the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America, which require us to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements as well as the reported amount of revenues and expenses during the reporting periods. Actual results could differ from these estimates.

### NOTE 2 - EARNINGS PER SHARE

The following table presents the computation of basic and diluted weighted average shares used in the per-share calculations:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2001	2000	2001	2000
	----	----	----	----
(In thousands)				
Income before cumulative effect of accounting changes.....	\$ 62,768	\$ 48,280	\$118,813	\$101,676
Preferred dividends - Series C .....	8,593	7,770	16,996	15,368
	-----	-----	-----	-----
Net income applicable to common stockholders before cumulative effect of accounting changes .....	54,175	40,510	101,817	86,308
Cumulative effect of accounting changes, net .....	--	--	14,499	3,438
	-----	-----	-----	-----
Net income applicable to common stockholders .....	\$ 54,175	\$ 40,510	\$ 87,318	\$ 82,870
	=====	=====	=====	=====
Weighted-average common shares outstanding .....	62,788	58,838	62,547	58,400
Adjustments for dilutive securities:				
Assumed conversion of convertible preferred stock .....	34,845	29,164	34,570	29,164
	-----	-----	-----	-----
Basic common shares (1) .....	97,633	88,002	97,117	87,564
Assumed exercise of outstanding stock options .....	2,208	3,566	1,938	3,554
	-----	-----	-----	-----
Diluted common shares .....	99,841	91,568	99,055	91,118
	=====	=====	=====	=====

(1) In accordance with an announcement of the Financial Accounting Standards Board's Staff at the Emerging Issues Task Force meeting in April,



## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

2001, codified as EITF Topic No. D-95 ("Topic D-95"), the Company revised its computation of basic earnings per common share (EPS). As required by Topic D-95, the dilutive effect of the Company's Series C Convertible Preferred Stock is now included in the computation of basic EPS, utilizing the if-converted method. The Series C Convertible Preferred Stock participates in dividends on an as-converted basis with the Company's common stock. For all periods presented, there is no impact to diluted earnings per share. The Company restated the basic EPS amounts for the three- and six-month periods ended June 30, 2000 to be consistent with the revised methodology. Before the impact of Topic D-95, basic earnings per common share would have been \$0.86, \$0.69, \$1.40 and \$1.42 for the three- and six-month periods ended June 30, 2001 and 2000, respectively.

### NOTE 3 - ACCOUNTING CHANGES

During the quarter ended March 31, 2001 we adopted Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities," which establishes accounting and reporting standards for derivative instruments. SFAS 133 requires enterprises to recognize all derivatives as either assets or liabilities in the statement of financial position and to measure those instruments at fair market value. This statement is effective for all quarters of fiscal years beginning after June 15, 2000. As a result of the adoption of SFAS 133 effective January 1, 2001 we marked our derivatives to market value and recognized a one-time, non-cash, after-tax charge to earnings of \$14.5 million. This one-time charge is reflected as a "Cumulative effect of accounting change" in the consolidated statements of income for the six months ended June 30, 2001.

We use derivatives to assist us in achieving our strategy of balanced asset and liability interest rate exposure. Our principal market risk is due to changes in interest rates. Our primary managed assets are credit card loans, which are virtually all priced at rates indexed to the variable Prime Rate. We fund credit card loans through a combination of cash flows from operations, asset securitizations, bank loans, subsidiary bank deposits, long-term debt and equity issuances. The majority of this funding is indexed to variable rate LIBOR. We seek to minimize the impact of changes in interest rates primarily by matching asset and liability repricings. We enter into interest rate cap, floor and swap agreements to hedge the cash flow, fair value and earnings impact of fluctuating market interest rates on the spread between the floating rate loans and the floating and fixed rate debt issued to fund the loans.

In connection with the issuance of term asset-backed securities by the Metris Master Trust ("trust"), we enter into term interest rate cap agreements with highly rated bank counterparties to effectively cap the potentially negative impact to us from increases in the floating interest rate of the securities. These agreements are for original terms ranging from two to ten years and are scheduled to terminate between February 2002 and January 2010. The contracted strike rate on the interest rate caps were above the current market interest rates at December 31, 2000 and June 30, 2001. Therefore, these caps are considered ineffective in hedging the interest rate movements. SFAS 133 required us to reduce the carrying value of these caps to their current market values. The reduction related to the adoption of SFAS 133 effective January 1, 2001 was recorded as a one-time, non-cash, after-tax charge to earnings of \$14.7 million. This one-time charge is included in the "Cumulative effect of accounting change" in the consolidated statements of income for the six months ended June 30, 2001. The adjustment to increase the carrying value of the caps for the three- and six-month periods ended June 30, 2001 was recorded as a non-cash, pre-tax benefit of \$6.7 million and \$3.0 million, respectively, to "Net securitization and credit card servicing income" in the consolidated statements of income.

We also enter into interest rate swap agreements to hedge a portion of our fixed rate deposits. The interest rate swaps are designated as fair value hedges

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

under SFAS 133. At adoption, the change in the fair value of the swaps exceeded the change in fair value of the fixed rate deposits. This difference of \$0.2 million was recorded as a one-time, non-cash, after-tax benefit to earnings. This one-time benefit is included in the "Cumulative effect of accounting change" in the consolidated statements of income for the six months ended June 30, 2001. The interest rate swaps were substantially effective in offsetting changes in the fair value of the hedged CD portfolio during the six months ended June 30, 2001. These interest rate swap agreements are for original terms ranging from one to two years and are scheduled to terminate between April 2002 and January 2003.

During the quarter ended March 31, 2000 we adopted Staff Accounting Bulletin ("SAB") No. 101, "Revenue Recognition in Financial Statements," for our debt waiver products. This SAB formalized the accounting for services sold where the right to a full refund exists, requiring all companies to defer recognition of revenues until the cancellation period is complete. Previously, we recognized half of the revenues in the month billed and half in the following month. We now recognize all of the revenue the month following completion of the cancellation period. This change resulted in a one-time, non-cash net charge to earnings of \$3.4 million, which is reflected as a "Cumulative effect of accounting change" in the consolidated statements of income for the six months ended June 30, 2000. Because we have applied the provisions of this SAB to our membership programs since 1998, before the SEC formalized its guidance, no adjustment was required for our membership services revenues.

### NOTE 4 - ALLOWANCE FOR LOAN LOSSES

The activity in the allowance for loan losses is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2001	2000	2001	2000
	----	----	----	----
(In thousands)				
Balance at beginning of period	\$ 786,798	\$ 645,089	\$ 763,975	\$ 619,028
Provision for loan losses ....	114,682	98,215	202,411	186,008
Provision for loan losses (1)	193,178	114,387	373,241	231,064
Loans charged off .....	(297,071)	(196,552)	(569,152)	(390,042)
Recoveries .....	28,554	15,982	55,666	31,063
	-----	-----	-----	-----
Net loans charged off .....	(268,517)	(180,570)	(513,486)	(358,979)
	-----	-----	-----	-----
Balance at end of period .....	\$ 826,141	\$ 677,121	\$ 826,141	\$ 677,121
	=====	=====	=====	=====

(1) Amounts are included in "Net securitization and credit card servicing income."

### NOTE 5 - SEGMENTS

We operate in two principal areas: consumer lending products and

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

enhancement services. Our consumer lending products are primarily unsecured and secured credit cards, including the Direct Merchants Bank MasterCard(R) and Visa(R). Our credit card accountholders include customers obtained from third-party lists and other customers for whom general credit bureau information is available.

We market our enhancement services, including (i) debt waiver protection for unemployment, disability, and death; (ii) membership programs such as card registration, purchase protection and other club memberships; and (iii) third-party insurance, directly to our credit card customers and customers of third parties. We currently administer our extended service plans sold through a third-party retailer, and the customer pays the retailer directly. In addition, we develop customized targeted mailing lists from information contained in our databases for use by unaffiliated companies in their own product solicitation efforts that do not directly compete with our efforts.

We have presented the segment information reported below on a managed basis. We use this basis to review segment performance and to make operating decisions. To do so, the income statement and balance sheet are adjusted to reverse the effects of securitizations. Presentation on a managed basis is not in conformity with generally accepted accounting principles. The elimination column in the segment table includes adjustments to present the information on an owned basis as reported in the financial statements of this quarterly report.

We do not allocate the expenses, assets and liabilities attributable to corporate functions to the operating segments, such as employee compensation, data processing services and communications, third-party servicing expenses, and other expenses including occupancy, depreciation and amortization, professional fees, and other general and administrative expenses. We include these expenses in the reconciliation of the income before income taxes and cumulative effect of accounting changes for the reported segments to the consolidated total. We do not allocate capital expenditures for leasehold improvements, capitalized software and furniture and equipment to operating segments. There were no operating assets located outside of the United States for the periods presented.

Our enhancement services operating segment pays a fee to our consumer lending products segment for successful marketing efforts to the consumer lending products segment's cardholders at a rate similar to those paid to our other third parties. Our enhancement services segment reports interest income and the consumer lending products segment reports interest expense at our weighted-average borrowing rate for the excess cash flow generated by the enhancement services segment and used by the consumer lending products segment to fund the growth of cardholder balances.

	Three Months Ended June 30, 2001 ----			
	Consumer Lending Products -----	Enhancement Services -----	Reconciliation (a) -----	Consolidated -----
Interest income.....	\$ 481,540	\$ 3,202	\$ (312,535) (b)	\$ 172,207

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Interest expense.....	129,361	--	(85,048) (b)	44,313
	-----	-----	-----	-----
Net interest income .....	352,179	3,202	(227,487)	127,894
Other revenue .....	160,240	82,900	34,309	277,449
Total revenue .....	641,780	86,102	(278,226)	449,656
Income before income taxes.....	173,672 (c)	55,058 (c)	(126,999) (d)	101,731
Total assets .....	\$9,777,687	\$ 138,076	\$ (5,959,431) (e)	\$3,956,332

Three Months Ended June 30,  
2000

	Consumer Lending Products -----	Enhancement Services -----	Reconciliation(a) -----	Consolidated -----
Interest income.....	\$ 376,022	\$ 2,697	\$ (262,960) (b)	\$ 115,759
Interest expense.....	122,768	--	(93,986) (b)	28,782
	-----	-----	-----	-----
Net interest income .....	253,254	2,697	(168,974)	86,977
Other revenue .....	119,452	63,984	54,587	238,023
Total revenue .....	495,474	66,681	(208,373)	353,782
Income before income taxes.....	138,611 (c)	42,666 (c)	(102,659) (d)	78,618
Total assets .....	\$ 7,737,289	\$ 150,025	\$ (5,174,697) (e)	\$ 2,712,617

Six Months Ended June 30,  
2001

	Consumer Lending Products -----	Enhancement Services -----	Reconciliation (a) -----	Consolidated -----
Interest income .....	\$ 948,360	\$ 6,822	\$ (613,246) (b)	\$ 341,936
Interest expense .....	273,291	--	(181,143) (b)	92,148

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Net interest income .....	675,069	6,822	(432,103)	249,788
Other revenue .....	285,611	161,164	58,862	505,637
Total revenue .....	1,233,971	167,986	(554,384)	847,573
Income before income taxes and cumulative effect of accounting changes..	331,251 (c)	109,737 (c)	(248,127) (d)	192,861
Total assets .....	\$9,777,687	\$ 138,076	\$ (5,959,431) (e)	\$3,956,332

Six Months Ended June 30,  
2000

	Consumer Lending Products	Enhancement Services	Reconciliation (a)	Consolidated
Interest income .....	\$ 735,524	\$ 4,902	\$ (526,866) (b)	\$ 213,560
Interest expense .....	237,502	--	(184,612) (b)	52,890
Net interest income .....	498,022	4,902	(342,254)	160,670
Other revenue .....	244,705	123,600	111,190	479,495
Total revenue .....	980,229	128,502	(415,676)	693,055
Income before income taxes and cumulative effect of accounting changes..	283,092 (c)	84,543 (c)	(201,768) (d)	165,867
Total assets .....	\$ 7,737,289	\$ 150,025	\$ (5,174,697) (e)	\$ 2,712,617

(a) The reconciliation column includes: intercompany eliminations; amounts not allocated to segments; and adjustments to the amounts reported on a managed basis to reflect the effects of securitization.

(b) The reconciliation to consolidated owned interest revenue and interest expense includes the elimination of \$3.2 million, \$2.7 million, \$6.8 million and \$4.9 million of intercompany interest received by the enhancement services segment from the consumer lending products segment for the three months ended June 30, 2001 and 2000 and the six months ended June 30, 2001 and 2000, respectively.

(c) Income before income taxes (and cumulative effect of accounting changes) includes intercompany commissions paid by the enhancement services segment to the consumer lending products segment for successful marketing efforts to consumer lending products cardholders of \$3.0 million, \$4.1 million, \$6.2 million and \$4.4 million for the three months ended June 30, 2001 and 2000 and the six months ended June 30, 2001 and 2000, respectively.

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

(d) The reconciliation to the owned income before income taxes and cumulative effect of accounting changes includes: unallocated costs related to employee compensation; data processing and communications; third-party servicing expenses; and other expenses. The majority of these expenses, although not allocated for the internal segment reporting used by management, relate to the consumer lending products segment.

(e) Total assets include the assets attributable to corporate functions not allocated to operating segments and the removal of investors interests in securitized loans to present total assets on an owned basis.

NOTE 6 - DEBT AND DEPOSITS

We have a credit facility that consists of a \$170 million revolving credit facility and a \$100 million term loan which mature in July 2003 and June 2003, respectively. At June 30, 2001 and December 31, 2000 we had outstanding borrowings of \$100 million under the term loan facility with weighted-average interest rates of 7.3% and 9.9%, respectively. There were no outstanding borrowings under the revolving credit facility for these periods. At June 30, 2001 we were in compliance with all financial covenants under the credit facility.

Direct Merchants Bank issues certificates of deposit of \$100,000 or more. As of June 30, 2001 and December 31, 2000, \$2.1 billion of CDs were outstanding with original maturities ranging from six months to five years and three months to five years, respectively. These CDs pay fixed interest rates ranging from 4.2% to 7.6% and 5.4% to 7.6%, respectively.

We have various indirect subsidiaries which have not guaranteed the senior notes or credit facility. The following condensed consolidating financial statements of the Company, the guarantor subsidiaries and the non-guarantor subsidiaries are presented for purposes of complying with SEC reporting requirements. Separate financial statements of the guarantor subsidiaries and the non-guarantor subsidiaries are not presented because management has determined that the subsidiaries' financial statements would not be material to investors.

METRIS COMPANIES INC.  
Supplemental Consolidating Balance Sheet  
June 30, 2001  
(Dollars in thousands)  
Unaudited

	Metris Companies Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Elim
	-----	-----	-----	-----
Assets:				
Cash and cash equivalents .....	\$ 1,725	\$ 935	\$ 682,723	\$
Net retained interests in loans				
securitized .....	(3,009)	--	504,015	
Credit card loans .....	60,045	--	1,994,550	

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Property and equipment, net .....	--	85,103	39,160	
Deferred income taxes .....	(3,438)	8,613	102,006	
Purchased portfolio premium .....	248	--	82,631	
Other receivables due from credit card securitizations, net.....		17	167,665	
Other assets .....	13,651	33,687	194,807	
Investment in subsidiaries .....	1,768,597	1,658,571	--	(3,4
	-----	-----	-----	-----
Total assets .....	\$ 1,837,836	\$ 1,788,262	\$ 3,767,557	\$ (3,4
	=====	=====	=====	=====
Liabilities:				
Deposits .....	\$ (1,000)	\$ --	\$ 2,175,945	\$
Debt .....	345,470	877	9,990	
Accounts payable .....	6,120	14,996	120,541	
Deferred income .....	8,602	31,155	175,262	
Accrued expenses and other liabilities.....	468,617	(27,363)	(372,752)	
	-----	-----	-----	-----
Total liabilities .....	827,809	19,665	2,108,986	
	-----	-----	-----	-----
Total stockholders' equity .....	1,010,027	1,768,597	1,658,571	(3,4
	-----	-----	-----	-----
Total liabilities and stockholders' equity.....	\$ 1,837,836	\$ 1,788,262	\$ 3,767,557	\$ (3,4
	=====	=====	=====	=====

METRIS COMPANIES INC.  
Supplemental Consolidating Balance Sheet  
December 31, 2000  
(Dollars in thousands)  
Unaudited

	Metris Companies Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Elimina
	-----	-----	-----	-----
Assets:				
Cash and cash equivalents .....	\$ 64,869	\$ 10,658	\$ 445,913	\$
Net retained interests in loans securitized .....	311	--	1,382,518	
Credit card loans .....	2,232	--	1,053,848	
Property and equipment, net .....	--	77,693	50,702	
Deferred income taxes .....	(2,415)	17,104	131,656	
Purchased portfolio premium .....	248	--	95,289	
Other receivables due from credit card securitizations, net.....	14	84	186,596	
Other assets .....	13,806	41,946	173,583	(10
Investment in subsidiaries .....	1,588,918	1,442,295	--	(3,031
	-----	-----	-----	-----
Total assets .....	\$ 1,667,983	\$ 1,589,780	\$ 3,520,105	\$ (3,041

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

	=====	=====	=====	=====
Liabilities:				
Deposits .....	\$ (1,000)	\$ --	\$ 2,107,199	\$
Debt .....	345,024	880	10,162	
Accounts payable .....	259	14,536	73,993	(5)
Deferred income .....	12,718	49,934	178,170	(5)
Accrued expenses and other liabilities.....	427,429	(64,488)	(291,714)	
Total liabilities .....	784,430	862	2,077,810	(10)
Total stockholders' equity .....	883,553	1,588,918	1,442,295	(3,031)
Total liabilities and stockholders' equity .....	\$ 1,667,983	\$ 1,589,780	\$ 3,520,105	\$ (3,041)
	=====	=====	=====	=====

METRIS COMPANIES INC.  
Supplemental Consolidating Statements of  
Three Months Ended June 30, 2001  
(Dollars in thousands)  
Unaudited

	Metris Companies Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminati
	-----	-----	-----	-----
Net Interest (Expense)				
Income.....	\$ (25,386)	\$ (2,162)	\$ 155,442	\$ --
Provision for loan losses .....	1,013	--	113,669	--
Net Interest (Expense)				
Income After Provision for Loan Losses.....	(26,399)	(2,162)	41,773	--
Other Operating Income:				
Net securitization and credit card servicing income.....	2,378	--	117,334	--
Credit card fees, interchange and other credit card income.....	(1,562)	16,085	60,314	--
Enhancement services revenues.....	--	14,083	68,817	--
	816	30,168	246,465	--
Other Operating Expense:				
Credit card account and other product solicitation and marketing expenses.....	--	4,364	47,117	--
Employee compensation .....	342	53,815	1,958	--



Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Data processing services and communications .....	2	(22,399)	44,538	—
Warranty and debt waiver underwriting and claims servicing expense.....	--	323	7,927	—
Credit card fraud losses .....	--	--	2,200	—
Purchased portfolio premium amortization .....	--	--	7,418	—
Other .....	52	25,825	15,448	—
	-----	-----	-----	-----
	396	61,928	126,606	—
	-----	-----	-----	-----
(Loss) Income Before Income Taxes, Equity in Income of Subsidiaries and Cumulative Effect of Accounting Change.....	(25,979)	(33,922)	161,632	—
Income taxes .....	(9,881)	(13,940)	62,784	—
Equity in income of subsidiaries.....	78,866	98,848	--	(177,711)
	-----	-----	-----	-----
Net Income .....	\$ 62,768	\$ 78,866	\$ 98,848	\$ (177,711)
	=====	=====	=====	=====

METRIS COMPANIES INC.  
Supplemental Consolidating Statements of Income  
Three Months Ended June 30, 2000  
(Dollars in thousands)  
Unaudited

	Metris Companies Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminati
	-----	-----	-----	-----
Net Interest (Expense)				
Income .....	\$ (20,834)	\$ (1,227)	\$ 109,038	\$
Provision for loan losses .....	(7)	--	98,222	
	-----	-----	-----	-----
Net Interest (Expense) Income After Provision for Loan Losses.....	(20,827)	(1,227)	10,816	
	-----	-----	-----	-----
Other Operating Income:				
Net securitization and credit card servicing income.....	2,378	24	118,107	
Credit card fees, interchange and other credit card income.....	(1,649)	(238)	55,417	
Enhancement services revenues.....	--	11,385	52,599	
	-----	-----	-----	-----
	729	11,171	226,123	
	-----	-----	-----	-----

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Other Operating Expense:				
Credit card account and other product solicitation and marketing expenses.....	--	2,878	33,438	
Employee compensation .....	--	35,902	6,880	
Data processing services and communications .....	--	(19,109)	39,928	
Warranty and debt waiver underwriting and claims servicing expense.....	--	24	6,736	
Credit card fraud losses .....	1	--	2,430	
Purchased portfolio premium amortization.....	--	--	5,225	
Other .....	56	15,471	18,307	
	-----	-----	-----	-----
	57	35,166	112,944	
	-----	-----	-----	-----
(Loss) Income Before				
Income Taxes and Equity in Income of Subsidiaries.....	(20,155)	(25,222)	123,995	
Income taxes .....	(7,789)	(9,802)	47,929	
Equity in income of subsidiaries.....	60,646	76,066	--	(136,7
	-----	-----	-----	-----
Net Income .....	\$ 48,280	\$ 60,646	\$ 76,066	\$ (136,7
	=====	=====	=====	=====

METRIS COMPANIES INC.  
Supplemental Consolidating Statements of  
Six Months Ended June 30, 2001  
(Dollars in thousands)  
Unaudited

	Metris Companies Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminati
	-----	-----	-----	-----
Net Interest (Expense)				
Income.....	\$ (60,937)	\$ (3,592)	\$ 314,317	\$
Provision for loan losses .....	1,217	--	201,194	
	-----	-----	-----	-----
Net Interest (Expense)				
Income After Provision for Loan Losses.....	(62,154)	(3,592)	113,123	
	-----	-----	-----	-----
Other Operating Income:				
Net securitization and credit card servicing income.....	4,756	--	202,048	

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Credit card fees, interchange and other credit card income.....	(2,851)	9,297	131,223	
Enhancement services revenues.....	--	31,201	129,963	
	-----	-----	-----	-----
	1,905	40,498	463,234	
	-----	-----	-----	-----
Other Operating Expense:				
Credit card account and other product solicitation and marketing expenses.....	--	10,484	81,762	
Employee compensation .....	342	97,226	13,283	
Data processing services and communications .....	2	(52,932)	97,450	
Warranty and debt waiver underwriting and claims servicing expense.....	--	490	14,439	
Credit card fraud losses .....	--	--	4,851	
Purchased portfolio premium amortization .....	--	--	15,246	
Other .....	90	44,287	33,133	
	-----	-----	-----	-----
	434	99,555	260,164	
	-----	-----	-----	-----
(Loss) Income Before Income Taxes, Equity in Income of Subsidiaries and Cumulative Effect of Accounting Change.....	(60,683)	(62,649)	316,193	
Income taxes .....	(23,242)	(25,910)	123,200	
Equity in income of subsidiaries.....	141,755	178,494	--	(320,2
	-----	-----	-----	-----
Income Before Cumulative Effect of Accounting Change.....	104,314	141,755	192,993	(320,2
Cumulative effect of accounting change, net .....	--	--	14,499	
	-----	-----	-----	-----
Net Income .....	\$ 104,314	\$ 141,755	\$ 178,494	\$ (320,2
	=====	=====	=====	=====

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Six Months Ended June 30, 2000  
(Dollars in thousands)  
Unaudited

	Metris Companies Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	El
	-----	-----	-----	-----
Net Interest (Expense)				
Income.....	\$ (32,881)	\$ (1,798)	\$ 195,349	\$
Provision for loan losses .....	(22)	--	186,030	
	-----	-----	-----	-----
Net Interest (Expense) Income After Provision for Loan Losses	(32,859)	(1,798)	9,319	
	-----	-----	-----	-----
Other Operating Income:				
Net securitization and credit card servicing income.....	4,764	(4)	246,808	
Credit card fees, interchange and other credit card income.....	(3,197)	870	106,654	
Enhancement services revenues.....	--	27,719	95,881	
	-----	-----	-----	-----
	1,567	28,585	449,343	
	-----	-----	-----	-----
Other Operating Expense:				
Credit card account and other product solicitation and marketing expenses.....	--	10,648	57,810	
Employee compensation .....	--	70,773	15,781	
Data processing services and communications .....	--	(37,853)	79,297	
Warranty and debt waiver underwriting and claims servicing expense.....	--	818	12,674	
Credit card fraud losses .....	3	--	4,569	
Purchased portfolio premium amortization .....	--	--	10,192	
Other .....	93	33,462	30,023	
	-----	-----	-----	-----
	96	77,848	210,346	
	-----	-----	-----	-----
(Loss) Income Before Income Taxes, Equity in Income of Subsidiaries and Cumulative Effect of Accounting Change.....	(31,388)	(51,061)	248,316	
Income taxes .....	(12,147)	(20,140)	96,478	
Equity in income of subsidiaries.....	117,479	148,400	--	(2)
	-----	-----	-----	-----
Income Before Cumulative Effect of Accounting Change .....	98,238	117,479	151,838	(2)
Cumulative effect of accounting change, net .....	--	--	3,438	

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Net Income .....	\$ 98,238	\$ 117,479	\$ 148,400	\$ (2
	=====	=====	=====	=====

METRIS COMPANIES INC.  
Supplemental Condensed Consolidating Statement  
Six Months Ended June 30, 2001  
(Dollars in thousands)  
Unaudited

	Metris Companies Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries
	-----	-----	-----
Operating Activities:			
Net cash (used in) provided by operating activities.....	\$ (77,889)	\$ (69,120)	\$ 411,919
	-----	-----	-----
Investing Activities:			
Net proceeds from sales and repayments of securitized loans .....	--	--	692,051
Net loans originated .....	(57,267)	--	(812,855)
Dispositions of (additions to) property and equipment.....	--	(14,636)	10,646
	-----	-----	-----
Net cash (used in) provided by investing activities	(57,267)	(14,636)	(110,158)
	-----	-----	-----
Financing Activities:			
Net increase (decrease) in debt .....	95,081	73,890	(168,700)
Net increase in deposits .....	--	--	68,746
Cash dividends paid .....	(1,847)	--	--
Net (decrease) increase in equity .....	(21,222)	143	35,003
	-----	-----	-----
Net cash provided by (used in) financing activities .....	72,012	74,033	(64,951)
	-----	-----	-----
Net (decrease) increase in cash and cash equivalents .....	(63,144)	(9,723)	236,810
Cash and cash equivalents at beginning of period .....	64,869	10,658	445,913
	-----	-----	-----
Cash and cash equivalents at end of period .....	\$ 1,725	\$ 935	\$ 682,723
	=====	=====	=====

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

METRIS COMPANIES INC.  
 Supplemental Condensed Consolidating Statement  
 Six Months Ended June 31, 2001  
 (Dollars in thousands)  
 Unaudited

	Metris Companies Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries
	-----	-----	-----
Operating Activities:			
Net cash (used in) provided by operating activities.....	\$ (86,740)	\$ (49,918)	\$ 361,577
	-----	-----	-----
Investing Activities:			
Net proceeds from sales and repayments of securitized loans .....	--	--	(34,075)
Net loans collected (originated).....	2,043	--	(563,492)
Additions to property and equipment .....	--	(17,550)	(23,618)
	-----	-----	-----
Net cash provided by (used in) investing activities .....	2,043	(17,550)	(621,185)
	-----	-----	-----
Financing Activities:			
Net increase (decrease) in debt .....	96,452	17,723	(113,731)
Net increase in deposits .....	--	--	469,592
Cash dividends paid .....	(1,137)	--	--
Net (decrease) increase in equity .....	(16,615)	50,529	2
	-----	-----	-----
Net cash provided by financing activities .....	78,700	68,252	355,863
	-----	-----	-----
Net (decrease) increase in cash and cash equivalents.....	(5,997)	784	96,255
Cash and cash equivalents at beginning of period.....	43,619	309	150,505
	-----	-----	-----
Cash and cash equivalents at end of period .....	\$ 37,622	\$ 1,093	\$ 246,760
	=====	=====	=====

ITEM 2.

METRIS COMPANIES INC. AND SUBSIDIARIES  
 MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
 FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis provides information management believes to be relevant to understanding the financial condition and results of operations of Metris Companies Inc. ("MCI") and its subsidiaries, including Direct Merchants Credit Card Bank, N.A. ("Direct Merchants Bank"), which may be referred to as "we," "us," "our" and the "Company." This discussion should be read in conjunction with the following documents for a full understanding of our financial condition and results of operations: Management's Discussion and Analysis of Financial Condition and Results of Operations in our 2000 Annual Report to Shareholders; our annual report on Form 10-K for the fiscal year ended December 31, 2000; and our Proxy Statement for the 2001 Annual Meeting of Shareholders. In addition, this discussion should be read in conjunction with our quarterly report on Form 10-Q for the period ended June 30, 2001, of which this commentary is a part, and the condensed consolidated financial statements

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

and related notes thereto.

### Results of Operations

Net income for the three months ended June 30, 2001 was \$62.8 million, up from \$48.3 million for the second quarter of 2000. Diluted earnings per share for the three months ended June 30, 2001 was \$0.63 compared to \$0.53 per share for the second quarter of 2000. The increase in net income is the result of increases in net interest income and other operating income, partially offset by increases in the provision for loan losses and other operating expenses. These increases are largely attributable to the growth in average managed loans to \$9.9 billion for the second quarter 2001 from \$7.6 billion for the second quarter 2000, an increase of 29%, and growth in total credit card accounts to 4.6 million at June 30, 2001, from 4.1 million at June 30, 2000. Enhancement services revenue also increased 30% to \$82.9 million for the second quarter of 2001 compared to the same period in 2000.

Net income for the six months ended June 30, 2001 was \$104.3 million, up from \$98.2 million for the first six months of 2000. Net income reported for the six-month periods ended June 30, 2001 and 2000 includes \$14.5 million and \$3.4 million, respectively, of cumulative effect of accounting changes described below. Without these items, reported earnings would have been \$118.8 million and \$101.7 million for the six-month periods ended June 30, 2001 and 2000, respectively. Diluted earnings per share for the six-months ended June 30, 2001 was \$1.05 compared to \$1.08 for the same period in 2000. Without the impact of the cumulative effect of accounting changes, diluted earnings per share would have been \$1.20 and \$1.12 for the six months ended June 30, 2001 and 2000, respectively. The increase in net income is the result of increases in net interest income and other operating income, partially offset by increases in the provision for loan losses and other operating expenses. These increases are largely attributable to the growth in average managed loans to \$9.6 billion for the six months ended June 30, 2001 from \$7.5 billion for the same period in 2000, an increase of 29%, along with the previously discussed growth in credit card accounts. Enhancement services revenue also increased 30% to \$161.2 million for the six months ended June 30, 2001 compared to the same period in 2000.

During the quarter ended March 31, 2001 we adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities," which establishes accounting and reporting standards for derivative instruments. SFAS 133 requires enterprises to recognize all derivatives as either assets or liabilities in the statement of financial position and to measure those instruments at fair value. Prior to SFAS 133, we amortized the costs of interest rate contracts on a straight-line basis over the expected life of the contract. The adoption of SFAS 133 resulted in a one-time, non-cash, after-tax charge to earnings of \$14.5 million reflected as a "Cumulative effect of accounting change" in the consolidated statements of income for the six months ended June 30, 2001.

During the quarter ended March 31, 2000 we adopted Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements," for our debt waiver products. This SAB formalized the accounting for services sold where the right to a full refund exists, requiring all companies to defer recognition of revenues until the cancellation period is complete. Previously, we recognized half of the revenues in the month billed and half in the following month. We now recognize all of the revenue the month following completion of the cancellation period. This change resulted in a one-time, non-cash net charge to earnings of \$3.4 million, which is reflected as a "Cumulative effect of accounting change" in the consolidated statements of income for the six months ended June 30, 2000. Because we have applied the provisions of this SAB to our membership programs since 1998, before the SEC formalized its guidance, no adjustment was required for our membership services revenues.

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

In September 2000 the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," which replaces SFAS No. 125, and revises the standards for accounting for securitizations and transfers of financial assets and collateral and requires certain disclosures. It requires enterprises to recognize, upon transfer of financial assets, the financial and servicing assets it controls and the liabilities it has incurred, derecognize financial assets when control has been surrendered, and derecognize liabilities when extinguished. This statement is effective for transfers and servicing of financial assets and extinguishment of liabilities occurring after March 31, 2001. The statement is effective for recognition and reclassification of collateral and for disclosures related to securitization transactions and collateral for fiscal years ending after December 15, 2000. We implemented the disclosure requirements in our 2000 Annual Report to comply with the new standard. The adoption of the accounting portion of the new standard did not have a material impact on our financial statements.

### Managed Loan Portfolio

We analyze our financial performance on a managed loan portfolio basis. To do so, we adjust the income statement and balance sheet to reverse the effects of securitization. Our discussion of revenues, where applicable, and provision for loan losses includes comparisons to amounts reported in our consolidated statements of income ("owned basis"), as well as on a managed basis.

Our managed loan portfolio is comprised of credit card loans, retained interests in loans securitized and the investors' share of securitized credit card loans. The investors' share of securitized credit card loans is not an asset of the Company. Therefore, we do not show it on our consolidated balance sheets. The following tables summarize our managed loan portfolio:

	June 30, 2001 ----	December 31, 2000 ----	June 30, 2000 ----
(Dollars in thousands)			
Period-end balances:			
Credit card loans:			
Credit card loans .....	\$ 2,312,652	\$ 1,179,203	\$ 543,836
Retained interests in loans securitized .....	1,069,090	2,023,681	1,815,047
Investors' interests in securitized loans .....	6,762,272	6,070,224	5,484,238
Total managed loan portfolio .	\$10,144,014	\$ 9,273,108	\$ 7,843,121

	Three Months Ended June 30, -----		Six Months End June 30, -----
	2001 ----	2000 ----	2001 ----



Edgar Filing: METRIS COMPANIES INC - Form 10-Q

(Dollars in thousands)

Average balances

Credit card loans:

Credit card loans .....	\$1,548,810	\$ 453,780	1,424,470
Retained interests in loans securitized .....	1,928,464	1,851,563	1,986,275
Investors' interests in securitized loans .....	6,376,798	5,306,617	6,214,612
	-----	-----	-----
Total managed loan portfolio..	\$9,854,072	\$7,611,960	\$9,625,357
	=====	=====	=====

Impact of Credit Card Securitizations

The following table provides a summary of the effects of credit card securitizations on selected line items of our statements of income for each of the periods presented, as well as selected financial information on both an owned and managed loan portfolio basis:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2001	2000	2001	2000
	----	----	----	----
(Dollars in thousands)				
Statements of Income				
(owned basis):				
Net interest income .....	\$ 127,894	\$ 86,977	\$ 249,788	\$ 160,670
Provision for loan losses ..	114,682	98,215	202,411	186,008
Other operating income .....	277,449	238,023	505,637	479,495
Other operating expense ....	188,930	148,167	360,153	288,290
	-----	-----	-----	-----
Income before income taxes and cumulative effect of accounting changes .....	\$ 101,731	\$ 78,618	\$ 192,861	\$ 165,867
	=====	=====	=====	=====
Adjustments for				
Securitizations:				
Net interest income .....	\$ 227,487	\$ 168,974	\$ 432,103	\$ 342,254
Provision for loan losses ..	193,178	114,387	373,241	231,064
Other operating income .....	(34,309)	(54,587)	(58,862)	(111,190)
Other operating expense ....	--	--	--	--
	-----	-----	-----	-----
Income before income taxes and cumulative effect of accounting changes .....	\$ --	\$ --	\$ --	\$ --
	=====	=====	=====	=====

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

### Statements of Income

(managed basis):

Net interest income .....	\$ 355,381	\$ 255,951	\$ 681,891	\$ 502,924
Provision for loan losses ..	307,860	212,602	575,652	417,072
Other operating income .....	243,140	183,436	446,775	368,305
Other operating expense .....	188,930	148,167	360,153	288,290
	-----	-----	-----	-----
Income before income taxes and cumulative effect of accounting changes .....	\$ 101,731	\$ 78,618	\$ 192,861	\$ 165,867
	=====	=====	=====	=====

	Three Months Ended June 30, -----		Six Month June -----	
	2001 ----	2000 ----	2001 ----	2000 ----

(Dollars in thousands)

#### Other Data:

##### Owned Basis:

Average interest-earning assets ..	\$ 3,765,165	\$ 2,475,510	\$ 3,776,734	\$
Return on average assets (1) .....	6.6%	7.5%	6.3%	
Return on average total equity (1)	25.9%	26.9%	25.5%	
Net interest margin (2) .....	13.6%	14.1%	13.3%	

##### Managed Basis:

Average interest-earning assets ..	\$ 10,141,963	\$ 7,782,127	\$ 9,991,346	\$
Return on average assets (1) .....	2.5%	2.5%	2.4%	
Return on average total equity (1)	25.9%	26.9%	25.5%	
Net interest margin (2) .....	14.1%	13.2%	13.8%	

(1) Amounts for the six-month period ended June 30, 2001 are shown before the impact of the adoption of SFAS 133.

(2) Net interest margin is equal to annualized net interest income divided by average interest-earning assets.

### Net Interest Income

Net interest income consists primarily of interest earned on our credit card loans, less interest expense on borrowings to fund the loans. Managed net interest income for the three- and six-month periods ended June 30, 2001 was \$355.4 million and \$681.9 million compared to \$256.0 million and \$502.9 million for the same periods in 2000. The increase in net interest income is primarily due to \$2.4 billion and \$2.3 billion increases in managed interest-earning assets and increases in net interest margin to 14.1% and 13.8% from 13.2% and 13.2% in the same periods in 2000. The managed net interest margin increase is primarily due to lower cost of funds resulting from decreases in LIBOR. Financing costs as a percentage of borrowings for the second quarter and year-to-date periods of 2001 were 5.7% and 6.2% compared with 7.1% and 7.0% in the same periods of 2000.

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Analysis of Average Balances, Interest and Average Yields and Rates

The following tables provide an analysis of interest income and expense, net interest spread, net interest margin and average balance sheet data for the three- and six-month periods ended June 30, 2001 and 2000:

	2001		Three Months Ended June 30,	
	Average Balance -----	Interest -----	Yield/ Rate ----	Average Balance -----
(Dollars in thousands)				
Owned Basis				
Assets:				
Interest-earning assets:				
Federal funds sold .....	\$ 31,013	\$ 329	4.3%	\$ 110,300
Short-term investments .....	256,878	3,176	5.0%	59,867
Credit card loans and retained interests in loans securitized .....	3,477,274	168,702	19.5%	2,305,343
Total interest-earning assets	\$ 3,765,165	\$ 172,207	18.3%	\$ 2,475,510
Other assets .....	831,526	--	--	770,797
Allowances for loan losses ..	(808,087)	--	--	(661,743)
Total assets .....	\$ 3,788,604	--	--	\$ 2,584,564
Liabilities and Equity:				
Interest-bearing liabilities:				
Deposits .....	\$ 2,061,761	\$ 32,936	6.4%	\$ 1,104,424
Debt .....	360,910	11,377	12.6%	350,899
Total interest-bearing liabilities .....	\$ 2,422,671	\$ 44,313	7.3%	\$ 1,455,323
Other liabilities .....	394,004	--	--	408,204
Total liabilities .....	2,816,675	--	--	1,863,527
Stockholders' equity .....	971,929	--	--	721,037
Total liabilities and equity	\$ 3,788,604	--	--	\$ 2,584,564
Net interest income and interest margin (1) .....				
Net interest rate spread (2)	--	\$ 127,894	13.6%	--
	--	--	11.0%	--
Managed Basis				
Credit card loans .....	\$ 9,854,072	\$ 478,034	19.5%	\$ 7,611,960
Total interest-earning assets	10,141,963	481,540	19.0%	7,782,127

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Total interest-bearing liabilities .....	8,799,469	126,159	5.7%	6,761,940
Net interest income and interest margin (1) .....	--	\$ 355,381	14.1%	--
Net interest rate spread (2)	--	--	13.3%	--

(1) We compute net interest margin by dividing annualized net interest income by average total interest-earning assets.

(2) The net interest rate spread is the annualized yield on average interest-earning assets minus the annualized funding rate on average interest-bearing liabilities.

	Six Months Ended June 30,			
	2001			
	Average Balance	Interest	Yield/ Rate	Average Balance
	-----	-----	----	-----
(Dollars in thousands)				
Owned Basis				
Assets:				
Interest-earning assets:				
Federal funds sold .....	\$ 97,425	\$ 2,640	5.5%	\$ 103,492
Short-term investments .....	268,564	7,072	5.3%	70,501
Credit card loans and retained interests in loans securitized .....	3,410,745	332,224	19.6%	2,132,270
	-----	-----	----	-----
Total interest-earning assets	\$ 3,776,734	\$ 341,936	18.3%	\$ 2,306,263
Other assets .....	818,830	--	--	752,518
Allowances for loan losses ..	(794,649)	--	--	(655,698)
	-----			-----
Total assets .....	\$ 3,800,915	--	--	\$ 2,403,083
	=====			=====
Liabilities and Equity:				
Interest-bearing liabilities:				
Deposits .....	\$ 2,095,898	\$ 69,559	6.7%	\$ 993,286
Debt .....	360,954	22,589	12.6%	351,899
	-----	-----	----	-----
Total interest-bearing liabilities .....	\$ 2,456,852	\$ 92,148	7.6%	\$ 1,345,185
Other liabilities .....	403,547	--	--	370,241
	-----			-----
Total liabilities .....	2,860,399	--	--	1,715,426
Stockholders' equity .....	940,516	--	--	687,657
	-----			-----
Total liabilities and equity	\$ 3,800,915	--	--	\$ 2,403,083
	=====			=====
Net interest income and interest margin (1) .....	--	\$ 249,788	13.3%	--
Net interest rate spread (2)	--	--	10.7%	--

Managed Basis

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Credit card loans .....	\$ 9,625,357	\$ 938,647	19.7%	\$ 7,482,178
Total interest-earning assets	9,991,346	948,360	19.1%	7,656,171
Total interest-bearing liabilities .....	8,671,464	266,469	6.2%	6,695,094
Net interest income and interest margin (1) .....	--	\$ 681,891	13.8%	--
Net interest rate spread (2)	--	--	12.9%	--

(1) We compute net interest margin by dividing annualized net interest income by average total interest-earning assets.

(2) The net interest rate spread is the annualized yield on average interest-earning assets minus the annualized funding rate on average interest-bearing liabilities.

### Other Operating Income

Other operating income contributes substantially to our results of operations, representing 68% and 67% of owned revenues for the three- and six-month periods ended June 30, 2001, respectively.

Other operating income increased \$39.4 million and \$26.1 million for the three- and six-month periods ended June 30, 2001 over the comparable periods in 2000. These increases are primarily due to the \$21.3 million and \$33.3 million increases in income generated from credit card fees, interchange and other credit card income, due to the growth in total accounts and loans in the managed credit card portfolio for the three- and six-month periods ended June 31, 2001 over the comparable periods in 2000. For the three- and six-month periods ended June 30, 2001, net securitization and credit card income decreased \$0.1 million and \$44.8 million, respectively, from the comparable periods in 2000. These decreases are primarily the result of the increased provision for securitized loans. For the six-month period ended June 30, 2000, other operating income included the \$12.1 million favorable impact related to the operational policy change in the billing of overlimit fees. This impact is reflected in net securitization and credit card servicing income and credit card fees, interchange and other credit card income in the consolidated statements of income.

Enhancement services revenues increased by \$18.9 million and \$37.6 million for the three- and six-month periods ended June 30, 2001. These increases reflect the strong sales of our debt waiver product and the increase in membership program revenues resulting from additional product offers to third-party cardholders. At June 30, 2001 combined active enhancement members totaled approximately 5.9 million.

### Other Operating Expense

Total other operating expenses for the three- and six-month periods ended June 30, 2001 increased \$40.8 million and \$71.9 million over the comparable periods in 2000, largely due to costs associated with the growth of our business activities. Employee compensation increased \$13.3 million and \$24.3 million for the three- and six-month periods ended June 30, 2001, due to increased staffing needs to support the increase in credit card accounts and enhancement services active member growth. Other expenses increased \$7.5 million and \$13.9 million for the three- and six-month periods ended June 30, 2001, due to increased fees associated with higher credit card volume. Also, credit card account and other product solicitation and marketing expenses increased \$15.2 million and \$23.8

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

million over the comparable periods in 2000, largely due to increased enhancement services marketing activity and costs associated with our credit card marketing activity, which resulted in over 510,000 new credit card accounts and 1.7 million new enhancement relationships during the first six months of 2001.

### Income Taxes

Our provision for income taxes, which includes both federal and state income taxes, represents an effective tax rate of 38.4% for the six-month period ended June 30, 2001, compared to 38.7% for the same period in 2000.

### Asset Quality

Our delinquency and net loan charge-off rates at any point in time reflect, among other factors, the credit risk of loans, the average age of our various credit card account portfolios, the success of our collection and recovery efforts, and general economic conditions. The average age of our credit card portfolio affects the stability of delinquency and loss rates. In order to minimize losses, we continue to focus our resources on refining our credit underwriting standards for new accounts, and on collections and post charge-off recovery efforts. At June 30, 2001, 49% of managed accounts and 31% of managed loans were less than 24 months old.

For the quarter ended June 30, 2001, our managed net charge-off ratio was 10.9% compared to 9.5% for the quarter ended June 30, 2000. For the six months ended June 30, 2001, the net charge-off rate stood at 10.8% compared to 9.6% for the six months ended June 30, 2000. Without the impact of purchase accounting related to acquired portfolios, the charge-off rate was 10.9% and 10.8% for the three- and six-month periods ended June 30, 2001 compared to 9.7% and 10.0% for the same periods of 2000. Our charge-offs without the impact of purchase accounting have been stable, with losses between 9.5% and 11.0% for the last 10 quarters. We believe, consistent with our statistical models and other credit analysis, that this rate will continue to fluctuate between this range over the next few quarters.

We use credit line analyses, account management and customer transaction authorization procedures to minimize loan losses. Our risk models determine initial credit lines at the time of solicitation and generally result in lower credit lines than the industry average. We manage credit lines on an ongoing basis and adjust them based on customer usage and payment patterns. To maximize profitability, we continually monitor customer accounts and initiate appropriate collection activities when an account is delinquent or overlimit.

### Delinquencies

Delinquencies not only have the potential to affect earnings in the form of net loan losses, but are also costly in terms of the personnel and other resources dedicated to their resolution. We monitor delinquency levels on a managed basis, since delinquency on either an owned or managed basis subjects us to credit loss exposure. A credit card account is contractually delinquent if we do not receive the minimum payment by the specified date on the cardholder's statement. It is our policy to continue to accrue interest and fee income on all credit card accounts, except in limited circumstances, until we charge off the account and all related loans, interest and other fees. The following table presents the delinquency trends of our credit card loan portfolio on a managed portfolio basis:

### Managed Loan Delinquency

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

	June 30, 2001 ----	% of Total -----	December 31, 2000 ----	% of Total -----	June 30, 2000 ----	% To ---
(Dollars in thousands)						
Managed loan portfolio	\$10,144,014	100%	\$ 9,273,108	100%	\$ 7,843,121	1
Loans contractually delinquent:						
30 to 59 days ...	253,328	2.5%	228,238	2.5%	189,322	2
60 to 89 days ...	190,381	1.9%	173,531	1.9%	137,513	1
90 or more days .	401,162	3.9%	365,963	3.9%	274,968	3
Total .....	\$ 844,871	8.3%	\$ 767,732	8.3%	\$ 601,803	7
	=====	=====	=====	=====	=====	=====

The increase in the managed delinquency rates over June 30, 2000 reflects a slight deterioration in the economy, increased delinquencies in our secured card portfolio and the adoption of recent FFIEC guidelines on re-aging accounts effective January 1, 2001, which required us to report an additional \$39.3 million of receivables as delinquent as of June 30, 2001. We intend to continue to focus our resources on our collection efforts to minimize the negative impact to net loan losses that results from increased delinquency levels.

Net Charge-Offs

Net charge-offs are the principal amount of losses from cardholders unwilling or unable to pay their loan balances, as well as bankrupt and deceased cardholders, less current period recoveries. Net charge-offs exclude accrued finance charges and fees, which are charged against the related income at the time of charge-off. The following table presents our net charge-offs for the periods indicated as reported in the consolidated financial statements and on a managed portfolio basis:

	Three Months Ended June 30, -----		Six Months Ended June 30, -----	
	2001 ----	2000 ----	2001 ----	2000 ----
(Dollars in thousands)				
Owned basis:				
Average loans and retained interests in loans securitized outstanding .....	\$3,477,274	\$2,305,343	\$3,410,745	\$2,132,2
Net charge-offs .....	92,494	55,723	173,931	103,2
Net charge-offs as a percentage of average loans outstanding (1)	10.7%	9.7%	10.3%	9
	=====	=====	=====	=====
Managed basis:				
Average loans outstanding .....	\$9,854,072	\$7,611,960	\$9,625,357	\$7,482,1
Net charge-offs .....	268,517	180,570	513,486	358,9

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Net charge-offs as a percentage of average loans outstanding(1) ...	10.9%	9.5%	10.8%	9
	=====	=====	=====	=====

(1) Annualized

Provision and Allowance for Loan Losses

We maintain an allowance for loan losses for both owned loans and the retained interest in loans securitized. The portion allocated to the retained interest in loans securitized represents our estimate of a valuation adjustment to report this asset in accordance with SFAS 140. For securitized loans, anticipated losses and related provisions for loan losses are reflected in the calculation of net securitization and credit card servicing income. We make provisions for loan losses in amounts necessary to maintain the allowance at a level estimated to be sufficient to absorb probable future loan losses, net of recoveries, inherent in the existing loan portfolio.

The provision for loan losses on a managed basis for the three- and six-month periods ended June 30, 2001 totaled \$307.9 million and \$575.7 million compared to provisions of \$212.6 million and \$417.1 million for the three- and six-month periods ended June 30, 2000. The increase for the three- and six-month periods ended June 30, 2001, as compared to the three- and six-month periods ended June 30, 2000, is reflective of the increase in loans and an increase in charge-offs. The allowance for loan losses on a managed basis was 8.1% at June 30, 2001 compared to 8.6% at June 30, 2000.

Derivatives Activities

We use derivative financial instruments for the purpose of managing our exposure to interest rate risks. We have a number of procedures in place to monitor and control both market and credit risk from these derivatives activities. Our senior management approves all derivative strategies and transactions.

Liquidity, Funding and Capital Resources

One of our primary financial goals is to maintain an adequate level of liquidity through active management of assets and liabilities. Because the pricing and maturing characteristics of our assets and liabilities change, liquidity management is a dynamic process, affected by changes in short- and long-term interest rates. We use a variety of financing sources to manage liquidity, refunding and interest rate risks.

June 30, 2001 ----	Weighted- Average Interest Rate -----	December 31, 2000 ----
--------------------------	--	------------------------------

Total period-end



## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

funding .....	\$10.3 billion	5.3%	\$9.4 billion
Bank loans .....	1.0%	7.2%	1.0%
Bank conduit securitizations..	--	--	2.3%
Long-term debt .....	2.5%	10.8%	2.7%
Equity .....	9.8%	--	9.4%
Deposits .....	21.1%	6.2%	22.4%
Metris Master Trust ...	65.6%	4.8%	62.2%
	-----		-----
	100.0%		100.0%
	=====		=====

We finance the growth of our credit card loan portfolio through cash flows from operations, asset securitizations, bank loans, subsidiary bank deposits, long-term debt and equity issuances.

During the three- and six-month periods ended June 30, 2001, we received net proceeds of \$591.9 million and \$692.0 million, respectively, from sales of credit card loans to the trust and conduits. We used cash generated from these transactions to fund credit card loan portfolio growth. During the three-month period ended June 30, 2000 we received net proceeds of \$248.0 million and distributed net proceeds of \$34.1 million during the six-month period ended June 30, 2000, to the trust and conduits. We financed these receivables on our balance sheet with the growth in our subsidiary bank deposit program.

Direct Merchants Bank issues certificates of deposit of \$100,000 or more. As of June 30, 2001 and December 31, 2000, \$2.1 billion of CDs were outstanding, with original maturities ranging from six months to five years and three months to five years, respectively. These CDs pay fixed interest rates ranging from 4.2% to 7.6% and 5.4% to 7.6%, respectively.

We have a \$170 million, three-year revolving credit facility and a \$100 million five-year term loan. At June 30, 2001 and December 31, 2000 we were in compliance with all financial covenants under these agreements. At June 30, 2001, and December 31, 2000, we had outstanding borrowings of \$100 million under the term loan facility and no outstanding borrowings under the revolving credit facility. We have also issued and sold \$150 million of 10.125% Senior Notes due 2006 and \$100 million of 10% Senior Notes due 2004.

As the portfolio of credit card loans grows our funding needs will increase accordingly. We believe that our cash flows from operations, asset securitizations, bank loans, subsidiary bank deposits, long-term debt and equity issuances will provide us with adequate liquidity for meeting anticipated cash needs, although no assurance can be given to that effect.

### Newly Issued Pronouncements

In July 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets," which establishes accounting and reporting standards for goodwill and other intangible assets. It requires enterprises to test these assets for impairment upon adoption of SFAS No. 142 as well as on an annual basis, and reduce the carrying amount of these assets if they are found to be impaired. Goodwill and other intangible assets with an indefinite useful life will no longer be amortized. Other intangible assets with an estimable useful life will continue to be amortized to their residual value over their useful lives. This statement is effective for goodwill and intangible assets included

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

on the balance sheet for all fiscal years beginning after December 15, 2001. The adoption of the new standard will not have a material impact on our financial statements.

### Forward-Looking Statements

This quarterly report contains some forward-looking statements. Forward-looking statements give our current expectations of future events. You will recognize these statements because they do not strictly relate to historical or current facts. Such statements may use words such as "anticipate," "estimate," "expect," "project," "intend," "think," "believe" and other words or terms of similar meaning in connection with any discussion of future performance of the Company. For example, these include statements relating to future actions, future performance of current or anticipated products, solicitation efforts, expenses, the outcome of contingencies such as litigation, and the impact of the capital markets on liquidity. From time to time, we also may provide oral or written forward-looking statements in other material released to the public.

Any or all of our forward-looking statements in this report and in any other public statements we make may turn out to be wrong. They can be affected by inaccurate assumptions or by known or unknown risks and uncertainties. Many factors, which can not be predicted with certainty, will be important in determining future results. Among such factors are the lack of seasoning of our credit card accounts which renders predictability of delinquencies more difficult, higher default and bankruptcy rates of our target market of moderate-income consumers, interest rate risks, risks associated with acquired portfolios, dependence on the securitization markets and other funding sources, state and federal laws and regulations that limit our business activities, product offerings and fees, privacy laws that could result in lower marketing revenue and penalties for non-compliance, and general economic conditions that can have a major impact on the performance of loans. Each of these factors and others are more fully discussed under the caption "Business--Risk Factors" contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2000. As a result of these factors, we cannot guarantee any forward-looking statements. Actual future results may vary materially. Also, please note that the factors we provide are those we think could cause our actual results to differ materially from expected and historical results. Other factors besides those listed here or in our 10-K for the year ended December 31, 2000 could also adversely affect us.

We undertake no obligations to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise. You are advised, however, to consult any further disclosure we make on related subjects in our periodic filings with the Securities and Exchange Commission. This discussion is provided to you as permitted by the Private Securities Litigation Reform Act of 1995.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the risk of loss from adverse changes in market prices and rates. Our principal market risk is due to changes in interest rates. This affects us directly in our lending and borrowing activities, as well as indirectly, as interest rates may impact the payment performance of our cardholders.

To manage our direct risk to market interest rates, management actively monitors the interest rates and the interest sensitive components of our owned and managed balance sheet to minimize the impact changes in interest rates have

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

on the fair value of assets, net income and cash flow. We seek to minimize the impact of changes in interest rates on us primarily by matching asset and liability repricings.

Our primary managed assets are credit card loans, which are virtually all priced at rates indexed to the variable Prime Rate. We fund credit card loans through a combination of cash flows from operations, asset securitizations, bank loans, subsidiary bank deposits, long-term debt and equity issuances. Our securitized loans are owned by a trust and bank-sponsored single-seller and multi-seller receivable conduits, which have committed funding primarily indexed to variable commercial paper rates and the London Interbank Offered Rate ("LIBOR"). The \$270 million bank credit facility has pricing that is also indexed to LIBOR or Prime Rate. The subsidiary bank deposits are issued at fixed interest rates. We have entered into interest rate swap agreements which effectively converted \$420 million of deposits to rates indexed to LIBOR. The long-term debt is at fixed interest rates. At June 30, 2001 approximately 10.7% of the trust and conduit funding of securitized receivables was funded with fixed rate securities.

In an interest rate environment with rates at or below current rates, 89.3% of the securitization funding for the managed loan portfolio is indexed to floating commercial paper and LIBOR rates. In an interest rate environment with rates significantly above current rates, the potentially negative impact on earnings of higher interest expense is mitigated by fixed rate funding and interest rate cap contracts.

The approach used by management to quantify interest rate risk is a sensitivity analysis, which management believes best reflects the risk inherent in our business. This approach calculates the impact on net income from an instantaneous and sustained change in interest rates by 200 basis points. Assuming no counteractive measures by management, a 200 basis point increase in interest rates affecting our floating rate financial instruments, including both debt obligations and loans, will result in an increase in net income of approximately \$17.2 million relative to a base case over the next 12 months; while a decrease of 200 basis points will result in a reduction in net income of approximately \$5.4 million. Our use of this methodology to quantify the market risk of financial instruments should not be construed as an endorsement of its accuracy or the accuracy of the related assumptions. In addition, this methodology does not take into account the indirect impact interest rates may have on the payment performance of our cardholders. The quantitative information about market risk is necessarily limited because it does not take into account operating transactions or other costs associated with managing immediate changes in interest rates.

### Part II. Other Information

#### Item 1. Legal Proceedings

We are a party to various legal proceedings resulting from the ordinary business activities relating to our operations. In July 2000 an Amended Complaint was filed in Hennepin County Court in Minneapolis, Minnesota against Metris Companies Inc. and our subsidiaries Metris Direct, Inc. and Direct Merchants Bank. The complaint seeks damages in unascertained amounts and purports to be a class action complaint on behalf of all cardholders who were issued a credit card by Direct Merchants Bank and were allegedly assessed fees or charges that the cardholder did not authorize. Specifically, the complaint alleges violations of the Minnesota

## Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Prevention of Consumer Fraud Act, the Minnesota Deceptive Trade Practices Act and breach of contract. We filed our answer to the complaint in August 2000. To date, the complaint has not been certified as a class action claim. We believe we have numerous substantive legal defenses to these claims and are continuing to vigorously defend the case. There can be no assurance that defense or resolution of these matters will not have a material adverse effect on our financial position.

On May 3, 2001, Direct Merchants Bank entered into a consent order with the Office of the Comptroller of the Currency ("OCC"). The consent order requires Direct Merchants Bank to pay approximately \$3.2 million in restitution to about 62,000 credit card customers who applied for and received a credit card in connection with a series of limited test marketing campaigns from March 1999 to June 1, 2000. Under the terms of the consent order, Direct Merchants Bank made no admission or agreement on the merits of the OCC's assertions. The restitution as required by the OCC consent order is reflected in our June 30, 2001 financial statements. We believe that Direct Merchants Bank's agreement with the OCC will not have a material adverse effect on the financial position of Metris Companies Inc. or Direct Merchants Bank.

The OCC also indicated that it is considering whether or not to pursue an assessment of civil money penalties and gave Direct Merchants Bank the opportunity to provide information to the OCC bearing on whether imposing a penalty would be appropriate and the severity of any penalty. The statutory provisions pursuant to which a civil money penalty could be assessed give the OCC broad discretion in determining whether or not a penalty will be assessed and, if so, the amount of the penalty. Because we are unable at this time to determine whether or not any civil money penalty will be assessed, there can be no assurance that the resolution of this matter will not have a material adverse effect on our financial position.

- Item 2. Changes in Securities  
Not applicable
- Item 3. Defaults Upon Senior Securities  
Not applicable
- Item 4. Submission of Matters to a Vote of Security Holders  
(a) The Company held its annual meeting of stockholders on May 9, 2001 and the following matters were voted on at that meeting.

(b) The directors listed below were elected at that meeting.

(1) The holders of our Common Stock elected three directors for a three-year term:

Walter Hoff  
Frank D. Trestman  
Ronald N. Zebeck

(2) The holders of our Series C Preferred Stock elected four directors for a one-year term:

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

C. Hunter Boll  
 Thomas M. Hagerty  
 David V. Harkins  
 Thomas H. Lee

(3) The following directors, previously elected by the holders of our Common Stock, continued their term of office after the meeting:

Lee R. Anderson, Sr.  
 John A. Cleary  
 Derek V. Smith  
 Edward B. Speno

(c) Matters Voted Upon

(1) The election of the following directors who will serve until their successors are elected and qualified, or their earlier death or resignation:

Director	For	Against	Withheld	Abstentions	Broker Non-Vote
Walter Hoff	55,882,884	None	1,256,856	None	None
Frank D. Trestman	55,878,869	None	1,260,871	None	None
Ronald Zebeck	47,571,238	None	9,568,502	None	None
C. Hunter Boll	33,693,403	None	None	None	None
Thomas M. Hagerty	33,693,403	None	None	None	None
David V. Harkins	33,693,403	None	None	None	None
Thomas H. Lee	33,693,403	None	None	None	None

(2) The approval of an increase in the number of shares reserved for issuance pursuant to the Metris Companies Inc. Amended and Restated Long-Term Incentive and Stock Option Plan from 15,000,000 to 17,000,000 shares.

For	Against	Withheld	Abstentions	Broker Non-Vote
76,120,065	14,589,353	None	123,725	None

(3) Ratification of the selection of KPMG LLP as independent auditors of the Company for 2001.

For	Against	Withheld	Abstentions	Broker Non-Vote
88,911,019	1,898,048	None	24,076	None

Item 5. Other Information  
 Not applicable

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits:

10.1 Transfer and Administration Agreement, dated June 15, 2001, among Direct Merchants Credit Card Bank, National Association, as Transferor, Variable Funding Capital

Edgar Filing: METRIS COMPANIES INC - Form 10-Q

Corporation, as a Conduit Investor, First Union National Bank, as a Committed Investor and as Liquidity Agent, and First Union Securities, Inc., as Deal Agent.

10.2 Amendment No. 1, dated as of April 26, 2001, to the Amended and Restated Pooling and Servicing Agreement dated as of July 30, 1998, among Metris Receivables, Inc., as Transferor, Direct Merchants Credit Card Bank, National Association, as Servicer, and U.S. Bank National Association, as Trustee (incorporated by reference to exhibit 4.2 to Metris Receivables, Inc.'s Registration Statement on Form S-3 (File No. 333-60530)).

10.3 Amendment No. 2, dated as of May 31, 2001, to the Amended and Restated Pooling and Servicing Agreement dated as of July 30, 1998, among Metris Receivables, Inc., as Transferor, Direct Merchants Credit Card Bank, National Association, as Servicer, and U.S. Bank National Association, as Trustee (incorporated by reference to exhibit 4.3 to Metris Receivables, Inc.'s Registration Statement on Form S-3 (File No. 333-60530)).

11 Computation of Earnings Per Share.

(b) Reports on Form 8-K: On May 4, 2001 the Company filed a Current Report on Form 8-K to report an agreement reached with the Office of the Comptroller of the Currency by Direct Merchants Bank, National Association, a subsidiary of Metris Companies Inc.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

METRIS COMPANIES INC.  
(Registrant)

Date: August 13, 2001

By: /s/ David D. Wesselink

-----  
David D. Wesselink  
Vice Chairman  
Principal Financial Officer

Date: August 13, 2001

By: /s/ Jeffrey D. Grosklags

-----  
Jeffrey D. Grosklags  
Senior Vice President, Assistant Secretary  
Principal Accounting Officer

