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CONTINENTAL AIRLINES INC /DE/

Form 8-K

July 07, 2004

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 8-K

CURRENT REPORT

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

Date of Report (Date of earliest event reported):
June 29, 2004

CONTINENTAL AIRLINES, INC.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation)	1-10323 (Commission File Number)	74-2099724 (IRS Employer Identification No.)
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1600 Smith Street, Dept. HQSEO, Houston, Texas (Address of principal executive offices)	77002 (Zip Code)
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(713) 324-2950
(Registrant's telephone number, including area code)

Item 7. Financial Statements and Exhibits.

(c) Exhibits. The Exhibit Index is hereby incorporated by reference. The documents listed on the Exhibit Index are filed as Exhibits with reference to the Registration Statement on Form S-3 (Registration No. 333-67886) of Continental Airlines, Inc. The Registration Statement and the final Prospectus Supplement, dated June 18, 2004, to the Prospectus, dated August 23, 2001, relate to the offering of Continental Airlines, Inc.'s Pass Through Certificates, Series 2004-ERJ1.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, Continental

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Airlines, Inc. has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

CONTINENTAL AIRLINES, INC.

July 7, 2004

By /s/ GERALD LADERMAN

Gerald Laderman
Senior Vice President - Finance and
Treasurer

EXHIBIT INDEX

- 1.1 Underwriting Agreement, dated June 18, 2004, among Citigroup Global Markets Inc. and Morgan Stanley & Co. Incorporated, as Underwriters, WestLB AG, New York Branch, as Depositary, Embraer-Empresa Brasileira de Aeronautica S.A. and Continental Airlines, Inc.
- 4.1 Trust Supplement No. 2004-ERJ1, dated as of June 29, 2004, between Wilmington Trust Company, as Trustee, and Continental Airlines, Inc. to Pass Through Trust Agreement, dated as of September 25, 1997
- 4.2 Revolving Credit Agreement (2004-ERJ1), dated as of June 29, 2004, between Wilmington Trust Company, as Subordination Agent, as Borrower, and WestLB AG, New York Branch, as Liquidity Provider
- 4.3 Revolving Credit Agreement (2004-ERJ1), dated as of June 29, 2004, between Wilmington Trust Company, as Subordination Agent, as Borrower, and Citicorp North America, Inc., as Liquidity Provider
- 4.4 Guarantee, dated June 29, 2004, by Citicorp, relating to the Revolving Credit Agreement (2004-ERJ1), dated as of June 29, 2004, between Wilmington Trust Company, as Subordination Agent, as Borrower, and Citicorp North America, Inc., as Liquidity Provider
- 4.5 Intercreditor Agreement, dated as of June 29, 2004, among Wilmington Trust Company, as Trustee, WestLB AG, New York Branch, and Citicorp North America, Inc., as Liquidity Providers, and Wilmington Trust Company, as Subordination Agent and Trustee
- 4.6 Deposit Agreement, dated as of June 29, 2004, between Wells Fargo Bank Northwest, National Association, as Escrow Agent, and WestLB AG, New York Branch, as Depositary
- 4.7 Escrow and Paying Agent Agreement, dated as of June 29, 2004, among Wells Fargo Bank Northwest, National Association, as Escrow Agent, Citigroup Global Markets Inc. and Morgan Stanley & Co. Incorporated, as Underwriters, Wilmington Trust Company, as Trustee, and Wilmington Trust Company, as Paying Agent

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- 4.8 Note Purchase Agreement, dated as of June 29, 2004, among Continental Airlines, Inc., Wilmington Trust Company, as Trustee, Subordination Agent and Paying Agent, and Wells Fargo Bank Northwest, National Association, as Escrow Agent
- 4.9 Form of Participation Agreement (Participation Agreement among Continental Airlines, Inc., as Lessee, [_____] , as Owner Participant, Wells Fargo Bank Northwest, National Association, as Owner Trustee and Lessor, Wilmington Trust Company, as Mortgagee, Subordination Agent and Trustee, and Embraer-Empresa Brasileira de Aeronautica S.A.) (Exhibit A to Note Purchase Agreement)
- 4.10 Form of Lease (Lease between Wells Fargo Bank Northwest, National Association, as Owner Trustee and Lessor, and Continental Airlines, Inc., as Lessee) (Exhibit B to Note Purchase Agreement)
- 4.11 Form of Indenture (Trust Indenture and Mortgage between Wells Fargo Bank Northwest, National Association, as Owner Trustee, and Wilmington Trust Company, as Mortgagee) (Exhibit C to Note Purchase Agreement)
- 4.12 Form of Trust Agreement ([Amended and Restated] Trust Agreement between [_____] , as Owner Participant, and Wells Fargo Bank Northwest, National Association, as Owner Trustee) (Exhibit E to Note Purchase Agreement)
- 4.13 9.558% Continental Airlines Pass Through Certificate, Series 2004-ERJ1, Certificate No. 1
- 23.1 Consent of Aviation Specialists Group, Inc., dated June 14, 2004
- 23.2 Consent of AvSolutions, Inc., dated June 14, 2004
- 23.3 Consent of BK Associates, Inc., dated June 14, 2004
- 23.4 Consent of Aviation Specialists Group, Inc., dated June 17, 2004
- 23.5 Consent of AvSolutions, Inc., dated June 17, 2004
- 23.6 Consent of BK Associates, Inc., dated June 17, 2004

total deposits of \$8.3 billion; total stockholders equity of \$917 million; and non-performing assets of \$49 million or 0.42% of total assets.

Banking Activities

Our primary business is banking. Our banking activities focus on:

the attraction of deposits from the general public through our retail branches;

the origination of loans, primarily loans secured by single family residential properties, which are either retained in our portfolio or sold in the secondary market;

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a strategy of providing exceptional customer service; and

continuing to offer products and services over the Internet and through our call center.

The types of loans we offer include:

adjustable rate residential mortgage loans, with rates tied primarily to the Eleventh District Cost of Funds Index (COFI) or the 12-month moving average of annual yields on actively traded U.S. Treasury securities to a constant maturity of one year (MTA), including subprime loans which carry higher interest rates;

fixed rate residential mortgage loans;

multi-family and commercial real estate loans, including loans secured by retail neighborhood shopping centers;

construction loans;

commercial loans; and

consumer loans.

We also invest in various securities to satisfy bank regulations regarding minimum levels of liquid assets and to provide a partial economic hedge against future value changes in our mortgage servicing rights.

Net income from our banking operations totaled \$8.4 million for the first three months of 2004 and \$95.5 million in 2003.

Real Estate Investment Activities

Downey is also involved in real estate investment, which is conducted primarily through the Bank's subsidiary, DSL Service Company. Activities include development, construction and property management relating to our portfolio of projects primarily within California but also in Arizona. Because of regulatory restrictions that have been placed on the Bank's real estate investment activities, we have reduced the amount of this business in recent years. Net income from our real estate investment and real estate joint venture activities was \$0.5 million for the first three months of 2004 and \$6.3 million in 2003.

Operating Strategy

Our operating strategy is to:

capitalize on our strong position in our core California market and expand customer usage of our Internet banking business;

focus on our residential lending expertise;

maintain our high lending standards and strong asset quality;

continue to strengthen our retail franchise;

continue to attract low-cost deposits from our retail customer base;

provide high-quality service to depositors and borrowers; and

improve our operating efficiency.

Our principal executive offices are located at 3501 Jamboree Road, Newport Beach, California, 92660, and our telephone number is (949) 854-0300.

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The information appearing above under the captions Banking Activities, Real Estate Investment Activities and Operating Strategy supersedes and replaces the information appearing under the same captions under Prospectus Summary in the accompanying prospectus.

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Anticipated Developments

We intend to use approximately \$123.7 million of the net proceeds from the sale of the notes to redeem all of our outstanding junior subordinated debentures, all of which are held by Downey Financial Capital Trust I, a special purpose entity (the Trust). Upon redemption of the junior subordinated debentures, the Trust will contemporaneously redeem all of its outstanding capital securities and common securities. In connection with our redemption of the junior subordinated debentures, we expect to incur an after-tax charge of approximately \$2.4 million. This charge represents the remaining unamortized issuance cost for the capital securities. See Use of Proceeds.

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The following table presents our summary consolidated financial data as follows:

the financial data as of and for the three months ended March 31, 2004 and 2003 has been derived from our unaudited consolidated quarterly financial statements which, in the opinion of management, include all adjustments, consisting of only normal, recurring adjustments, considered necessary for a fair presentation; and

the financial data as of, and for the years ended, December 31, 2003, 2002, 2001, 2000 and 1999 has been derived from our audited consolidated financial statements.

You should read the following financial information in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and related notes in our Annual Report on Form 10-K for the fiscal year ended December 31, 2003 and our Quarterly Report on Form 10-Q for the quarter ended March 31, 2004 that we have incorporated by reference into this prospectus supplement. See Where You Can Find More Information in this prospectus supplement. Our results of operations and financial condition as of and for the three months ended March 31, 2004 are not necessarily indicative of our results of operations or financial condition to be expected for any future period.

<i>(Dollars in thousands)</i>	Three Months Ended March 31,		Year Ended December 31,				
	2004	2003	2003	2002	2001	2000	1999
Income statement data							
Total interest income	\$ 120,795	\$ 147,297	\$ 522,450	\$ 633,038	\$ 808,381	\$ 784,360	\$ 533,751
Total interest expense	51,439	66,401	233,837	318,012	503,183	522,257	326,428
Net interest income	69,356	80,896	288,613	315,026	305,198	262,103	207,323
Provision for (reduction of) loan losses	1,804	(1,709)	(3,718)	939	2,564	3,251	11,270
Net interest income after provision for (reduction of) loan losses	67,552	82,605	292,331	314,087	302,634	258,852	196,053
Other income, net:							
Loan and deposit related fees	12,456	11,978	53,076	47,220	50,486	30,089	20,097
Real estate and joint ventures held for investment, net	926	943	9,835	10,250	3,885	8,798	19,302
Secondary marketing activities:							
Loan servicing income (loss), net	(14,245)	(13,686)	(27,060)	(39,629)	(11,373)	(3,628)	1,672
Net gains on sales of loans and mortgage-backed securities	1,372	19,763	61,436	45,860	22,432	3,297	14,806
Net gains on sales of mortgage servicing rights		5	23	331	934		
Net losses on trading securities			(10,449)				
Net gains (losses) on sales of investment securities	2,112	8	8	219	329	(106)	288
Gain on sale of subsidiary(a)						9,762	
Litigation award		2,452	2,851				
Other	332	579	1,222	2,803	2,215	2,714	3,268
Total other income, net	2,953	22,042	90,942	67,054	68,908	50,926	59,433
Operating expense:							
Total general and administrative expense	55,092	51,984	207,999	186,644	162,496	136,189	144,382

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Net operation of real estate acquired in settlement of loans	(72)	297	(929)	11	239	818	19
Amortization of excess cost over fair value of branch acquisitions(b)					457	462	474
Total operating expense	55,020	52,281	207,070	186,655	163,192	137,469	144,875
Income before income taxes	15,485	52,366	176,203	194,486	208,350	172,309	110,611
Income tax expense	6,573	22,149	74,462	82,193	88,169	73,058	46,807
Net income(a)	\$ 8,912	\$ 30,217	\$ 101,741	\$ 112,293	\$ 120,181	\$ 99,251	\$ 63,804

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<i>(Dollars in thousands)</i>	Three Months Ended March 31,		Year Ended December 31,				
	2004	2003	2003	2002	2001	2000	1999
Selected period-end balances							
Total assets	\$ 13,525,129	\$ 11,441,650	\$ 11,645,980	\$ 11,981,878	\$ 11,108,757	\$ 10,897,590	\$ 9,411,267
Loans and							
mortgage-backed securities	11,594,098	10,675,557	10,396,510	10,976,942	10,132,413	10,084,353	8,746,063
Deposits	8,817,173	8,997,558	8,293,758	9,238,350	8,619,566	8,082,689	6,562,761
Borrowings	3,059,112	1,424,561	2,253,022	1,747,795	1,646,423	2,102,283	2,246,491
Stockholders' equity	924,557	851,650	917,018	823,104	733,896	624,636	532,418
Loans serviced for others	9,167,834	8,535,480	9,313,948	8,316,236	5,805,811	3,964,462	2,923,778
Loan activity							
Loans originated	\$ 2,890,646	\$ 2,348,312	\$ 10,548,675	\$ 10,445,978	\$ 8,128,285	\$ 5,217,421	\$ 7,132,486
Loans and							
mortgage-backed securities purchased	65,537	92,738	706,949	1,497,645	216,214	19,775	49,669
Loans and							
mortgage-backed securities sold	678,746	1,624,166	6,581,856	7,103,861	4,553,944	1,662,600	2,386,958
Asset quality data							
Net charge-offs as a percentage of average loans							
	%	0.01%	0.01%	0.02%	0.01%	0.01%	0.06%
End of period:							
Total non-performing assets	\$ 53,595	\$ 75,400	\$ 48,631	\$ 79,814	\$ 92,632	\$ 54,974	\$ 39,194
Non-performing assets as a percentage of total assets							
	0.40%	0.66%	0.42%	0.67%	0.83%	0.50%	0.42%
Allowance for loan losses as a percentage of total loans							
	0.29	0.33	0.30	0.34	0.38	0.35	0.44
Allowance for loan losses as a percentage of non-performing loans							
	66.27	50.78	70.82	51.89	46.76	76.63	116.25
Performance ratios							
Effective interest rate spread							
	2.42%	2.86%	2.61%	2.91%	2.91%	2.65%	2.88%
Return on average assets(a)							
	0.30	1.03	0.89	1.00	1.11	0.97	0.85
Return on average equity(a)							
	3.88	14.41	11.65	14.42	17.81	17.17	12.70
Efficiency ratio(c)							
	77.18	52.23	56.70	50.23	43.93	46.23	58.41
Capital ratios							
Average stockholders equity to average assets							
	7.73%	7.16%	7.62%	6.93%	6.22%	5.65%	6.70%
Bank only end of period (d)							
Core and tangible capital							
	6.90	7.26	7.96	6.92	7.10	6.42	6.27
Risk-based capital							
	13.36	13.87	15.55	14.08	14.53	12.94	12.14
Leverage ratio							
	12.92	13.34	15.06	13.52	13.90	12.34	11.41

(a) In 2000, a \$5.6 million after-tax gain was recognized from the sale of Downey Auto Finance Corp. Excluding the gain, 2000 net income would have been \$93.6 million, the return on average assets would have been 0.92% and the return on average equity would have been 16.20%.

(b) During the fourth quarter of 2002, we adopted SFAS 147, which required us to cease the amortization of goodwill as of January 1, 2002.

(c)

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We define the efficiency ratio as our general and administrative expense expressed as a percentage of net interest income plus other income, excluding income associated with real estate held for investment, a litigation award and gain on sale of subsidiary.

- (d) For more information regarding these ratios see Management's Discussion and Analysis of Financial Condition and Results of Operations Financial Condition Regulatory Capital Compliance in our Annual Report on Form 10-K for the fiscal year ended December 31, 2003 and our Quarterly Report on Form 10-Q for the quarter ended March 31, 2004 incorporated by reference in this prospectus supplement.

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	to the Notes The notes will be effectively subordinated to the liabilities of our subsidiaries and to our secured indebtedness.
Ratings	The notes are expected to be rated Ba1 by Moody's Investors Service and BBB- by Standard & Poor's Ratings Services. See Description of the Notes Ratings.
Denominations and Form	The notes will be issued in denominations of \$1,000 and integral multiples of \$1,000. The notes will be issued in book-entry form and will be evidenced by one or more global certificates in fully registered form without coupons.
Trustee	Wilmington Trust Company
Covenants	<p>The Indenture pursuant to which the notes will be issued will contain covenants that will, in general:</p> <p>limit our ability to sell or otherwise dispose of or issue Voting Stock of a Principal Subsidiary Bank if, after giving effect to that transaction, we would own less than 80% of the outstanding shares of Voting Stock of that Principal Bank Subsidiary on a fully diluted basis; or</p> <p>limit our ability to create Liens upon more than 20% of the outstanding shares of Voting Stock of any Principal Subsidiary Bank.</p> <p>These covenants are subject to a number of significant exceptions and limitations and you should carefully review the information under Description of the Notes Certain Covenants and Description of the Notes Certain Definitions for further information about these covenants, including information about the exceptions and limitations to these covenants, and the definitions of the capitalized terms used above.</p>
Use of Proceeds	<p>We estimate that the net proceeds from the sale of the notes, after deducting underwriting discounts and our estimated offering expenses, will be approximately \$ million. We intend to use approximately \$123.7 million of the net proceeds from the sale of the notes to redeem all of our outstanding junior subordinated debentures, all of which are held by the Trust. Upon redemption of the junior subordinated debentures, the Trust will contemporaneously redeem all of its outstanding capital securities and common securities. See Prospectus Supplement Summary Downey Financial Corp. Anticipated Developments. We intend to use the remaining net proceeds for general corporate purposes, which may include advances to or investments in our subsidiaries, working capital and capital expenditures.</p>
Absence of a Public Market for the Notes	The notes will be a new issue of securities for which there is no established market. Accordingly, there can be no

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assurance that a market for the notes will develop or as to the liquidity of any market that may develop. The underwriters have advised us that they currently intend to make a market in the notes. However, they are not obligated to do so and any market making with respect to the notes may be discontinued without notice.

Issuance of Additional Notes

We may, without the consent of the holders of the notes, issue additional notes from time to time in the future. See Description of the Notes General.

Risk Factors

You should carefully review the information appearing in this prospectus supplement under the caption Risk Factors before making an investment decision.

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RISK FACTORS

Your investment in the notes will involve a number of risks. You should carefully consider the following discussion of risks, and the other information included or incorporated by reference in this prospectus supplement and the accompanying prospectus, before buying the notes.

Risks Relating to Downey

Our California business focus and economic conditions in California could adversely affect our operations.

Downey is headquartered in and its operations are concentrated in California. At March 31, 2004, approximately 94% of our total loans were secured by real estate located in California. As a result of this geographic concentration, our results depend largely upon economic and business conditions in this state. Deterioration of economic conditions in California could have a material adverse impact on the quality of our loan and real estate portfolios, the demand for our products and services and our results of operations and financial condition.

Significant changes in interest rates could adversely affect our performance and results of operations.

If interest rates vary substantially from present levels, our results may differ materially from recent levels. Changes in interest rates will influence the growth of loans, investments, deposits and borrowings and affect the rates received on loans and investment securities and paid on deposits and borrowings. Changes in interest rates also affect the value of our recorded mortgage servicing rights on loans we service for others, generally increasing in value as interest rates rise and declining as interest rates fall. If interest rates were to increase significantly, the economic feasibility of real estate investment activities also could be adversely affected. Accordingly, changes in interest rates could have a material adverse effect on our results of operations and financial condition.

We are subject to government regulation and federal monetary policy that could limit or restrict our activities, which could adversely affect our operations.

The financial services industry is subject to extensive federal and state supervision and regulation. Significant new laws or changes in, or repeals of, existing laws may adversely affect our results of operations. Further, federal monetary policy, particularly as implemented through the Federal Reserve System, significantly affects credit conditions for Downey, primarily through open market operations in United States government securities, the discount rate for borrowings and reserve requirements. A material change in these conditions could have a material adverse impact on our results.

Competition may adversely affect our performance.

The banking and financial services business in our market areas is highly competitive. The increasingly competitive environment is a result primarily of changes in regulation, changes in technology and product delivery systems, and continued consolidation among financial services providers. Increasing levels of competition in the banking and financial services businesses may reduce our market share, cause the prices we charge for our products to decline or cause the interest rates we are required to pay to attract deposits to increase. Our results may be adversely affected in future periods depending on the nature or level of competition.

If a significant number of borrowers, guarantors and related parties fail to perform as required by the terms of their loans, we will sustain losses.

A significant source of risk arises from the possibility that losses will be sustained because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loans. While we have adopted underwriting and loan quality monitoring systems, procedures and credit policies, including the establishment and review of the allowance for loan losses, such policies and procedures may not prevent losses that could materially affect our results.

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Risks Relating to the Notes

We are a holding company and our ability to service our debt, including the notes, depends upon cash provided to us by our primary subsidiary, the Bank.

The notes will be our obligation exclusively and will not be the obligation of, or guaranteed by, the Bank or any of our other subsidiaries. In addition, the notes are not savings accounts or deposits and are not insured by the Federal Deposit Insurance Corporation (the FDIC) or any other governmental agency or insurer. We are a holding company and we conduct substantially all of our operations through the Bank and its subsidiary, DSL Service Company. We derive substantially all of our revenues from, and substantially all of our operating assets are owned by, the Bank. As a result, our cash flow and our ability to service our debt, including the notes, depend primarily on the results of operations of the Bank and upon the ability of the Bank to provide us cash to pay amounts due on our obligations, including the notes. The Bank and our other subsidiaries are separate and distinct legal entities and have no obligation to make payments on the notes or to make any funds available to us for that purpose. In addition, dividends, loans or other distributions from our subsidiaries to us are or may be subject to legal, regulatory and contractual restrictions, are dependent upon results of operations of our subsidiaries, and are subject to other business considerations.

In that regard, various statutory and regulatory restrictions limit, directly or indirectly, the ability of the Bank to provide funds to us, whether as dividends, loans, investments in us or otherwise. For example, the Bank generally may not declare dividends or make any other capital distribution to us if, after the payment of such dividend or other distribution, it would fall within any of the three undercapitalized categories under the prompt corrective action standards established by the Office of Thrift Supervision (the OTS) and the other federal banking agencies pursuant to Section 38 of the Federal Deposit Insurance Act. A regulation of the OTS also limits the Bank's ability to pay dividends and make other capital distributions in a manner that depends upon the extent to which the Bank meets its regulatory capital requirements and other factors. Among other things, the Bank is required to obtain the prior approval of the OTS to pay dividends and make other capital distributions if the annual amount of the dividends and capital distributions exceeds its net income for that year to date added to its retained net income for the two preceding years. At March 31, 2004, the Bank could have paid approximately \$140 million in dividends to us without needing prior approval of the OTS. Further, applicable federal regulations require the Bank to give the OTS at least 30 days' advance notice of any proposed dividends or other capital distributions. Furthermore, the OTS may prohibit any dividend or other capital distribution that it determines would constitute an unsafe or unsound practice. As a consequence, the Bank's regulators could deem the payment of dividends by the Bank to us to be an unsafe or unsound practice, depending on the Bank's financial condition or otherwise, and prohibit such payments. If the Bank were unable to pay dividends to us, whether because of action by regulators or as a result of restrictions under applicable law or regulations, we would likely be unable to make debt service payments on the notes until such time as the Bank could again pay us dividends.

In addition to the regulation of dividends and other capital distributions, there are various statutory and regulatory limitations on the extent to which the Bank can finance or otherwise transfer funds to us or our non-banking subsidiaries, whether in the form of loans, extensions of credit, investments or asset purchases. The Director of the OTS may further restrict these transactions in the interests of safety and soundness.

As of March 31, 2004, the Bank met the capital and other requirements of a well capitalized institution under the OTS' prompt corrective action standards. There can be no assurance that the Bank will remain well capitalized in the future or that the OTS will not require the Bank to maintain higher levels of capital in light of the risk profile of its lending activities. As a result, the ability of the Bank to pay dividends and otherwise provide funds to us may be reduced, perhaps substantially, in the future.

For more information about these regulatory requirements, see Business Regulation Regulation of Downey and Business Regulation Regulation of the Bank in our Annual Report on Form 10-K for the fiscal year ended December 31, 2003, which is incorporated by reference in this prospectus supplement.

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The notes will be effectively subordinated to the liabilities of our subsidiaries and to our secured indebtedness.

Because of our holding company structure, the notes will be effectively subordinated to all existing and future indebtedness, trade payables, lease obligations and other liabilities of our subsidiaries, including deposit liabilities of the Bank. Therefore, our rights and the rights of our creditors, including the holders of the notes, to participate in the assets of any subsidiary upon the subsidiary's liquidation, conservatorship, receivership or reorganization will be subject to the prior claims of that subsidiary's creditors including, in the case of the Bank, the prior claims of the holders of its deposit liabilities, except (subject to the following discussion) to the extent that we may ourselves be a creditor with recognized claims against that subsidiary. In that regard, in the event that a receiver or conservator is appointed for any of our subsidiaries whose deposits are insured by the FDIC (our only subsidiary whose deposits are at present insured by the FDIC is the Bank), federal law grants the claims of holders of that subsidiary's deposit liabilities (including the FDIC as subrogee or transferee), and the claims of the receiver or conservator of that subsidiary for administrative expenses, priority over the claims of the subsidiary's general unsecured creditors. Thus, in the event of a conservatorship or receivership of the Bank or any other insured subsidiary, claims for its deposit liabilities and for the administrative expenses of the receiver or conservator would have a priority over any claims that we ourselves may have as a creditor of that subsidiary. Moreover, if we are a creditor of one of our subsidiaries, our claims would still be effectively subordinated to any security interests in, or mortgages or other liens on, the assets of that subsidiary and would be subordinate to any indebtedness of that subsidiary senior to that held by us. As of March 31, 2004, our subsidiaries had approximately \$12.5 billion of liabilities outstanding, including approximately \$8.8 billion of deposit liabilities of the Bank but excluding liabilities owed to us or other subsidiaries, to which the notes would be structurally subordinated.

The notes will also be effectively subordinated to any secured indebtedness we may incur in the future to the extent of the collateral pledged to secure that indebtedness. Downey Financial Corp. does not currently have any secured indebtedness.

The indenture that will govern the notes will not contain any limitation on the amount of indebtedness or other liabilities, including deposit liabilities, indebtedness and guarantees, that our subsidiaries and we may incur in the future.

It may be difficult for investors to sell their notes.

Investors may find it difficult to sell their notes because an active trading market for the notes may not develop. The notes will be a new issue of securities and there is currently no trading market for the notes. We do not intend to apply for the notes to be listed on any securities exchange or to arrange for the notes to be quoted on any quotation system. The underwriters have advised us that they currently intend to make a market in the notes, but they are not obligated to do so and the underwriters may discontinue any market making in the notes at any time in their sole discretion and without notice. Accordingly, we cannot assure investors that a trading market will develop for the notes or as to the liquidity of any trading market that may develop, that investors will be able to sell their notes at a particular time or that the prices that investors receive if and when they sell will be favorable.

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A WARNING ABOUT FORWARD-LOOKING INFORMATION

Downey has made forward-looking statements in this prospectus supplement and accompanying prospectus and in documents that are incorporated by reference herein and therein that are subject to risks and uncertainties. These statements are based on the beliefs and assumptions of management and on information available to management at the time these forward-looking statements were made. Forward-looking statements include the information concerning possible or assumed future operating results and financial condition appearing under Prospectus Supplement Summary and Risk Factors and statements preceded by, followed by or that include the words believes, expects, anticipates, intends, plans, estimates or similar expressions. Although we believe that our expectations are based on reasonable assumptions, actual results may differ materially from our expectations. Factors that could cause actual results to differ from expectations include those described under Risk Factors and the following:

General economic or business conditions, either nationally or in California, may be less favorable than expected, resulting in, among other things, a deterioration in credit quality or a reduced demand for credit;

Because our business is concentrated in California, changes in the economic conditions in the California market could adversely affect our operations;

Changes in the interest rate environment could adversely affect our banking and real estate investment activities;

Regulatory changes could have adverse effects on the financial services industry;

Significant increases in competitive pressures among depository and other financial institutions could adversely affect our operations;

Federal monetary policy changes could have adverse effects on the financial services industry; or

We could experience greater than anticipated losses on our loans because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loans.

Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Actual results may differ from expectations due to many factors beyond our ability to control or predict, including those described above and under Risk Factors. For these statements, Downey claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

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USE OF PROCEEDS

We estimate that the net proceeds from the sale of the notes, after deducting underwriting discounts and our estimated offering expenses, will be approximately \$ million. We intend to use approximately \$123.7 million of the net proceeds to redeem all of our outstanding junior subordinated debentures, all of which are held by Downey Financial Capital Trust I, a special purpose entity (the Trust). We intend to use the remaining proceeds for general corporate purposes, which may include advances to or investments in our subsidiaries, working capital and capital expenditures.

On July 23, 1999, the Trust issued \$120.0 million aggregate liquidation amount of its 10% capital securities in an underwritten public offering and contemporaneously sold \$3.7 million aggregate liquidation value of its 10% common securities to us. Proceeds from the offering of the capital securities and the sale of the Trust's common securities to us were used by the Trust to purchase \$123.7 million aggregate principal amount of junior subordinated debentures issued by us. The sole asset of the Trust is the junior subordinated debentures. The debentures carry an interest rate of 10% per annum and are due September 15, 2029.

We intend to redeem, in whole, the junior subordinated debentures on or shortly after July 23, 2004 before their maturity at a redemption price of 100% of their principal amount plus accrued and unpaid interest. Upon redemption of the junior subordinated debentures, the Trust will contemporaneously redeem all of its outstanding capital securities and common securities for an aggregate redemption price of \$123.7 million, plus accrued and unpaid distributions.

The capital securities and common securities pay quarterly cumulative cash distributions at an annual rate of 10% of the liquidation value of \$25 per security. We own all of the issued and outstanding common securities of the Trust and report them separately on our balance sheet. As a result, we will receive approximately \$3.7 million, plus accrued distributions, if any, when the common securities are redeemed by the Trust.

In connection with our redemption of the junior subordinated debentures, we expect to incur an after-tax charge of approximately \$2.4 million. This charge represents the remaining unamortized issuance costs for the capital securities.

Pending application of the net proceeds for the purposes described above, we may temporarily loan the net proceeds to the Bank.

Table of Contents**CAPITALIZATION**

The following table sets forth our consolidated total capitalization as of March 31, 2004 on an actual basis and as adjusted to give effect to the issuance and sale of the notes and the redemption of the junior subordinated debentures as described under Use of Proceeds.

This table should be read in conjunction with our consolidated financial statements and the related notes in our Annual Report on Form 10-K for the fiscal year ended December 31, 2003 and our Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2004 that we have incorporated by reference into this prospectus supplement.

(Dollars in Thousands, Except Per Share Amounts)	At March 31, 2004	
	Actual	As Adjusted
Borrowings		
Securities sold under agreements to repurchase	\$ 507,027	\$ 507,027
Federal Home Loan Bank advances and real estate notes	2,428,374	2,428,374
Junior subordinated debentures	123,711	
Senior notes offered hereby		
Total borrowings	3,059,112	
Stockholders equity		
Preferred stock, par value \$0.01 per share; authorized 5,000,000 shares; outstanding none		
Common stock, par value \$0.01 per share; authorized 50,000,000 shares; issued 28,235,022 shares	282	282
Additional paid-in capital	93,792	93,792
Accumulated other comprehensive income	1,753	1,753
Retained earnings(a)	839,898	837,501
Treasury stock, at cost, 281,275 shares	(11,168)	(11,168)
Total stockholders equity	924,557	922,160
Total capitalization	\$3,983,669	\$

- (a) The decline in the As Adjusted column reflects the after-tax charge associated with the remaining unamortized issuance costs for the capital securities issued by the Trust that will be recognized in our financial statements in connection with the redemption of the junior subordinated debentures as described under Use of Proceeds.

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The following table sets forth our ratio of earnings to fixed charges on a consolidated basis for the periods specified.

	Three Months Ended March 31, 2004	Year Ended December 31,				
		2003	2002	2001	2000	1999
Ratio of earnings to fixed charges:						
Excluding interest on deposits	1.80x	3.34x	3.60x	3.63x	2.20x	2.54x
Including interest on deposits	1.30x	1.73x	1.61x	1.41x	1.33x	1.33x

The ratio of earnings to fixed charges is calculated as follows:

$$\frac{(\text{income before income taxes}) + (\text{fixed charges}) - (\text{capitalized interest})}{(\text{fixed charges})}$$

Fixed charges, excluding interest on deposits, consist of:

interest on short-term borrowings and long-term debt;

amortization of debt expense;

capitalized interest; and

one-third of net rental expense, which we believe is representative of the interest factor.

Fixed charges, including interest on deposits, consist of all of the items listed immediately above plus interest on deposits.

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DESCRIPTION OF THE NOTES

The notes will be issued under an indenture dated as of November 15, 2000 (which is the Senior Indenture referred to in the accompanying prospectus), as amended and supplemented by a first supplemental indenture to be dated as of the closing date of this offering, between us and Wilmington Trust Company, as trustee. We refer to the indenture, as so amended and supplemented, as the Indenture. The terms of the Indenture include those stated in the Indenture and those made part of the Indenture by the Trust Indenture Act of 1939. The following summary of selected provisions of the Indenture and the notes is not complete and is subject to, and is qualified in its entirety by reference to, all the provisions of the Indenture and the notes. Copies of the Indenture and the form of certificate evidencing the notes are available or may be obtained from us as described in this prospectus supplement under Documents Incorporated by Reference and Where You Can Find More Information.

In this section, and in the section of the accompanying prospectus captioned Description of the Senior and Subordinated Debt Securities, references to Downey, we, our and us and similar references mean Downey Financial Corp. excluding, unless the context otherwise requires or otherwise expressly stated, its subsidiaries. Capitalized terms that are used in the following summary but not defined have the meanings given to those terms in the Indenture.

The notes offered by this prospectus supplement are a series of senior notes as described in the accompanying prospectus. The following description of the particular terms of the notes and the Indenture supplements, and to the extent inconsistent replaces, the description of the general terms and provisions of the senior notes and the Indenture contained in the accompanying prospectus.

General

The Indenture provides that we may issue debt securities (debt securities) under the Indenture from time to time in one or more series and permits us to establish the terms of each series of debt securities at the time of issuance. The Indenture does not limit the amount of debt securities that we may issue under the Indenture.

The notes will constitute a separate series of debt securities under the Indenture, initially limited to \$ in aggregate principal amount. Under the Indenture we may, without the consent of the holders of the notes, reopen this series and issue additional notes from time to time in the future, except that we may not issue any additional notes if an event of default under the Indenture has occurred and is continuing with respect to the notes or if we have effected satisfaction and discharge, defeasance or covenant defeasance of the notes as described below under Satisfaction and Discharge or Defeasance; Covenant Defeasance. The notes offered by this prospectus supplement and any additional notes we may issue in the future will constitute a single series of debt securities under the Indenture.

The notes will mature on , 2014. Interest on the notes will accrue from , 2004 at the rate of % per annum, payable semi-annually in arrears on and of each year, beginning on , 2004, to the persons in whose names the notes are registered at the close of business on or , as the case may be, next preceding those interest payment dates. As a result, the interest that is due and payable on any interest payment date, including any interest payment date that is also the maturity date or a redemption date, will be payable to the holders of the notes (or one or more predecessor notes) registered as such at the close of business on the relevant record date. Interest on the notes will be computed on the basis of a 360-day year consisting of twelve 30-day months. The information in this paragraph supercedes and replaces the information set forth under the caption Description of the Senior and Subordinated Debt Securities Payment of Principal and Interest and the first three paragraphs under the caption Description of the Senior and Subordinated Debt Securities Payment of Interest in the accompanying prospectus.

If an interest payment date, redemption date or maturity date of a note falls on a day that is not a business day, then the payment of principal, premium, if any, or interest, as the case may be, due in respect of that note on that date need not be made on that date, but may be made on the next succeeding business day with the

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same force and effect as if made on that interest payment date, redemption date or maturity date, as the case may be, and no interest will accrue for the period from that interest payment, redemption date or maturity date, as the case may be, to that next succeeding business day.

The notes will be denominated and payable in U.S. dollars. The notes will be issued in fully registered form without coupons in denominations of \$1,000 and integral multiples of \$1,000. The notes will be issued in book-entry form and will be evidenced by one or more global certificates, which we sometimes refer to as global notes, registered in the name of Cede & Co., as nominee of The Depository Trust Company (DTC). We sometimes refer to DTC or any successor depository for the notes as the depository. Purchasers of the notes will not be entitled to receive notes in definitive certificated form, which we sometimes refer to as certificated notes, registered in their names, except in the limited circumstances described below under Certificated Notes. See Book-Entry Issuance in the accompanying prospectus for additional information applicable to the depository arrangements.

In the event that certificated notes are issued in exchange for interests in global notes, the certificated notes may be presented for payment and surrendered for registration of transfer and exchange at our agency maintained for that purpose in the Borough of Manhattan, The City of New York, currently the office of the trustee's agent located at c/o Computershare Trust Company of New York, 88 Pine Street, New York, New York 10005, and in Wilmington, Delaware, currently the office of the trustee located at Rodney Square North, 1100 North Market Street, Wilmington, Delaware 19890. Under the Indenture, we will be required to maintain an office or agency in the Borough of Manhattan, The City of New York, where notes may be surrendered for registration of transfer, exchange and payment. Holders will not be required to pay any service charge for the registration of transfer or exchange of notes, other than any tax or other governmental charge payable in connection with the transfer or exchange.

Payment of interest on global notes will be made to DTC or its nominee. Payment of interest on notes in certificated form, if issued, will be made against presentation of those notes at the offices or agencies referred to in the preceding paragraph or, at our option, by mailing checks payable to the persons entitled to that interest to their addresses as they appear in the note register or by wire transfer.

The notes will not be entitled to the benefit of any sinking fund and will not be subject to repurchase, repayment or redemption by us at the option of the holders. Without limitation to the foregoing, the Survivor's Option described in the accompanying prospectus under Description of the Senior and Subordinated Debt Securities Survivor's Option will not be applicable with respect to the notes. The notes are not convertible or exchangeable for other securities.

The Indenture does not limit the amount of indebtedness or other liabilities that we or our subsidiaries may incur and, except to the limited extent described below under Certain Covenants and Merger, Consolidation and Transfer of Assets, the Indenture does not contain any provisions that are intended to protect holders of notes in the event of a highly-leveraged or similar transaction affecting us.

The notes will be subject to satisfaction and discharge, defeasance and covenant defeasance as described below under Satisfaction and Discharge and Defeasance; Covenant Defeasance.

Ranking

The notes will be our unsecured and unsubordinated obligations and will rank equally in right of payment with all of our other unsecured and unsubordinated indebtedness. The notes will rank senior in right of payment to our outstanding 10% junior subordinated debentures due 2029. See Use of Proceeds.

The notes will be our obligation exclusively and will not be the obligation of, or guaranteed by, any of our subsidiaries. In addition, the notes are not savings accounts or deposits and are not insured by the FDIC or any other governmental agency or insurer. We are a holding company and we conduct substantially all of our operations through the Bank and its subsidiary, DSL Service Company. Because of our holding company structure, the notes will be effectively subordinated to all existing and future indebtedness, trade payables, lease obligations and other liabilities of our subsidiaries, including deposit liabilities of the Bank. The notes will also be effectively subordinated to any secured indebtedness we may incur in the future to the extent of the

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collateral pledged to secure that indebtedness. See Risk Factors Risks Relating to the Notes We are a holding company and our ability to service our debt, including the notes, depends upon cash provided to us by our primary subsidiary, the Bank and Risk Factors Risks Relating to the Notes The notes will be effectively subordinated to the liabilities of our subsidiaries and to our secured indebtedness.

Ratings

The notes are expected to be rated Bal by Moody's Investors Service and BBB- by Standard & Poor's Rating Services. The rating of the notes should be evaluated independently from similar ratings on other types of securities. In addition, the credit ratings on the notes are subject to ongoing evaluation by credit rating agencies, and we cannot assure you that any such rating will not be changed or withdrawn by a rating agency in the future if, in its judgment, circumstances warrant. Moreover, a rating is not a recommendation to buy, sell or hold the notes, inasmuch as such rating does not comment as to market price or suitability for a particular investor.

Optional Redemption

The notes will be redeemable, in whole or from time to time in part, at the option of Downey on any date (each, a redemption date) at a redemption price equal to the greater of:

(a) 100% of the principal amount of the notes to be redeemed; and

(b) the sum of the present values of the remaining scheduled payments of principal and interest on the notes to be redeemed (exclusive of interest accrued to the applicable redemption date) discounted to such redemption date on a semiannual basis, assuming a 360-day year consisting of twelve 30-day months, at the Treasury Rate plus basis points, plus, in the case of both clause (a) and (b) above, accrued and unpaid interest on the principal amount of the notes being redeemed to such redemption date. Notwithstanding the foregoing, installments of interest on notes that are due and payable on an interest payment date falling on or prior to the relevant redemption date will be payable to the holders of such notes (or one or more predecessor notes) registered as such at the close of business on the relevant record date. Notwithstanding any statement in the accompanying prospectus to the contrary, a redemption date for the notes need not be an interest payment date.

Treasury Rate means, with respect to any redemption date for the notes:

(a) the yield, under the heading that represents the average for the immediately preceding week, appearing in the most recently published statistical release designated H.15(519) or any successor publication which is published weekly by the Board of Governors of the Federal Reserve System and which establishes yields on actively traded United States Treasury securities adjusted to constant maturity under the caption Treasury Constant Maturities, for the maturity corresponding to the Comparable Treasury Issue (if no maturity is within three months before or after the Final Maturity Date for the notes, yields for the two published maturities most closely corresponding to the Comparable Treasury Issue shall be determined and the Treasury Rate shall be interpolated or extrapolated from such yields on a straight-line basis, rounding to the nearest month); or

(b) if such release (or any successor release) is not published during the week preceding the calculation date or does not contain such yields, the rate per annum equal to the semiannual equivalent yield to maturity of the Comparable Treasury Issue, calculated using a price for the Comparable Treasury Issue (expressed as a percentage of its principal amount) equal to the Comparable Treasury Price for such redemption date.

The Treasury Rate shall be calculated on the third Business Day preceding the applicable redemption date. Notwithstanding any other provision in this prospectus supplement or the accompanying prospectus to the contrary, as used in the immediately preceding sentence and in the definition of Reference Treasury Dealer Quotations below, the term Business Day means each Monday, Tuesday, Wednesday, Thursday and

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Friday which is not a day on which banking institutions in The City of New York are authorized or obligated by law, regulation or executive order to close.

Comparable Treasury Issue means, with respect to any redemption date for the notes, the United States Treasury security selected by the Independent Investment Banker as having a maturity comparable to the remaining term of the notes to be redeemed that would be utilized, at the time of selection and in accordance with customary financial practice, in pricing new issues of corporate debt securities of comparable maturity to the remaining term of the notes to be redeemed.

Independent Investment Banker means, with respect to any redemption date for the notes, Credit Suisse First Boston LLC and its successors or J.P. Morgan Securities Inc. and its successors, whichever shall be selected by the trustee after consultation with Downey, or, if both such firms or the respective successors, if any, to such firms, as the case may be, are unwilling or unable to select the Comparable Treasury Issue, an independent investment banking institution of national standing appointed by the trustee after consultation with Downey.

Comparable Treasury Price means, with respect to any redemption date for the notes:

(a) the average of four Reference Treasury Dealer Quotations for such redemption date, after excluding the highest and lowest such Reference Treasury Dealer Quotations, or

(b) if the trustee obtains fewer than four such Reference Treasury Dealer Quotations, the average of all such quotations.

Reference Treasury Dealer means each of Credit Suisse First Boston LLC and J.P. Morgan Securities Inc. and their respective successors (provided, however, that if any such firm or any such successor, as the case may be, shall cease to be a primary U.S. Government securities dealer in New York City (a Primary Treasury Dealer), the trustee, after consultation with Downey, shall substitute therefor another Primary Treasury Dealer), and two other Primary Treasury Dealers selected by the trustee after consultation with Downey.

Reference Treasury Dealer Quotations means, with respect to each Reference Treasury Dealer and any redemption date for the notes, the average, as determined by the trustee, of the bid and asked prices for the Comparable Treasury Issue (expressed in each case as a percentage of its principal amount) quoted in writing to the trustee by such Reference Treasury Dealer at 5:00 p.m., New York City time, on the third Business Day preceding such redemption date.

Final Maturity Date means , 2014.

Notice of any redemption will be mailed at least 30 days but not more than 60 days before any redemption date to each holder of notes to be redeemed. If less than all the notes are to be redeemed at the option of Downey, the trustee will select, pro rata, by lot or in such other manner as it deems appropriate, the notes to be redeemed.

Unless Downey defaults in payment of the redemption price, on and after any redemption date interest will cease to accrue on the notes or portions thereof called for redemption on such redemption date.

The information under this caption Optional Redemption supersedes and replaces the information appearing in the sixth paragraph under the caption Description of the Senior and Subordinated Debt Securities Redemption and Repayment in the accompanying prospectus.

Certain Covenants

The following covenants will apply to the notes.

Limitation on Sale or Issuance of Voting Stock of a Principal Subsidiary Bank. Subject to the provisions described below under Merger, Consolidation and Transfer of Assets, Downey:

(a) will not, and will not cause or permit any Subsidiary to, directly or indirectly, sell, assign, transfer or otherwise dispose of or issue any shares of Voting Stock of, or any securities convertible into or

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exchangeable for or options, warrants or rights to subscribe for or purchase shares of Voting Stock of, any Principal Subsidiary Bank or any Subsidiary which owns, directly or through one or more other Subsidiaries, shares of Voting Stock of, or any securities convertible into or exchangeable for or options, warrants or rights to subscribe for or purchase shares of Voting Stock of, any Principal Subsidiary Bank, or

(b) cause or permit any Principal Subsidiary Bank, in any transaction or series of related transactions, to consolidate or merge with or into, or sell, lease, assign, transfer or otherwise convey all or substantially all of its properties and assets to, any other person (a Surviving Person),

unless the following conditions are satisfied:

(1) in the case of any transaction described in clause (a) above, such transaction is for not less than fair market value (as determined by the board of directors of Downey or of the Principal Subsidiary Bank or other Subsidiary, as the case may be, that is selling, assigning, transferring, disposing of or issuing the applicable shares, securities, options, warrants or rights, such determination to be evidenced by a resolution of such board of directors certified by the Secretary or an Assistant Secretary of Downey or of such Principal Subsidiary Bank or other Subsidiary, as the case may be, and delivered to the trustee, and which determination shall be conclusive) and, immediately after giving effect to such transaction and assuming the conversion or exchange, as the case may be, of all securities convertible into or exchangeable for and the exercise of any options, warrants or rights to subscribe for or purchase shares of Voting Stock of the applicable Principal Subsidiary Bank and all other Subsidiaries, Downey would own, directly or indirectly, not less than 80% of the outstanding shares of each class and series of Voting Stock of such Principal Subsidiary Bank, or

(2) in the case of any transaction described in clause (b) above, the Surviving Person is or will be (upon giving effect to such transaction) a Principal Subsidiary Bank and, immediately after giving effect to such transaction and assuming the conversion or exchange, as the case may be, of all securities convertible into or exchangeable for and the exercise of any options, warrants or rights to subscribe for or purchase shares of Voting Stock of such Surviving Person and all other Subsidiaries, Downey would own, directly or indirectly, not less than 80% of the outstanding shares of each class and series of Voting Stock of such Surviving Person and, immediately after giving effect to such transaction, no event of default under the Indenture and no event which, with notice or lapse of time or both, would become an event of default under the Indenture shall have occurred and be continuing;

provided, however, that the foregoing shall not prohibit any of the following:

(a) any sale, assignment, transfer or other disposition or issuance of such Voting Stock or other securities made, in the minimum amount required by law, to any person for the purpose of the qualification of such person to serve as a director of a Principal Subsidiary Bank; or

(b) any sale, assignment, transfer or other disposition or issuance of such Voting Stock or other securities made in compliance with an order of a court or regulatory authority of competent jurisdiction; or

(c) any sale, assignment, transfer or other disposition or issuance of shares of Voting Stock of, or securities convertible into or exchangeable for or options, warrants or rights to subscribe for or purchase shares of Voting Stock of,

(1) a Principal Subsidiary Bank, or

(2) any Subsidiary which owns, directly or through one or more other Subsidiaries, shares of Voting Stock of, or securities convertible into or exchangeable for or options, warrants or rights to subscribe for or purchase shares of Voting Stock of, any Principal Subsidiary Bank,

to Downey or a Subsidiary so long as, immediately after giving effect to such transaction and assuming the conversion or exchange, as the case may be, of all securities convertible into or exchangeable for and the exercise of any options, warrants or rights to subscribe for or purchase shares of Voting Stock of the

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applicable Principal Subsidiary Bank and all other Subsidiaries, Downey would own, directly or indirectly, not less than 80% of the outstanding shares of each class and series of Voting Stock of such Principal Subsidiary Bank; or

(d) the merger or consolidation of a Principal Subsidiary Bank with or into, or any sale, lease, assignment, transfer or other conveyance of all or substantially all of the properties and assets of any Principal Subsidiary Bank to, another Principal Subsidiary Bank or another Subsidiary (a Successor Subsidiary) which is or will be (upon giving effect to such transaction) a Principal Subsidiary Bank, so long as, immediately after giving effect to such transaction and assuming the conversion or exchange, as the case may be, of all securities convertible into or exchangeable for and the exercise of any options, warrants or rights to subscribe for or purchase shares of Voting Stock of such other Principal Subsidiary Bank or Successor Subsidiary, as the case may be, and all other Subsidiaries, Downey would own, directly or indirectly, not less than 80% of the outstanding shares of each class and series of Voting Stock of such other Principal Subsidiary Bank or Successor Subsidiary, as the case may be; or

(e) any sale, transfer or other disposition of all of the outstanding shares of Voting Stock of a Principal Subsidiary Bank owned, directly or indirectly, by Downey to, any merger of a Principal Subsidiary Bank into, any consolidation of a Principal Subsidiary Bank with, or any sale, lease, assignment, transfer or other conveyance of all or substantially all of the properties and assets of a Principal Subsidiary Bank to, any person that is not a Subsidiary, so long as all of the proceeds of such transaction are in cash and either

(x) within 180 days after such transaction, such proceeds are invested in one or more Principal Subsidiary Banks (including any existing Principal Subsidiary Bank or any other Subsidiary or person which in each case upon such investment becomes a Principal Subsidiary Bank) or

(y) within 180 days after such transaction, Downey has entered into a legally binding written agreement to invest such proceeds in one or more Principal Subsidiary Banks (including any existing Principal Subsidiary Bank or any other Subsidiary or person which in each case upon such investment will become a Principal Subsidiary Bank) but such investment has not been made because all regulatory or other similar approvals have not been obtained but are in the process of being obtained and such investment is made promptly after receipt of such approvals (provided that, if any such legally binding agreement is terminated or any such regulatory or other similar approvals are not obtained, Downey shall, within 90 days thereafter, invest such proceeds as described in clause (x) above),

and, in each case referred to in (x) and (y) above, the aggregate consolidated assets, determined in accordance with GAAP, of the Principal Subsidiary Bank or Banks, as the case may be, acquired or invested in or to be acquired or invested in (including any person which upon such investment becomes or would become, as the case may be, a Principal Subsidiary Bank) would be at least equal to 80% of the consolidated assets, determined in accordance with GAAP, of the Principal Subsidiary Bank being disposed of; provided, however, that if, within 180 days after the disposition of a Principal Subsidiary Bank, Downey acquires a person which upon such acquisition becomes a Principal Subsidiary Bank in accordance with the foregoing provisions of this paragraph (e) (including the consolidated asset requirement) in exchange for Downey's Common Stock or Preferred Stock with a fair market value at least equal to the proceeds of the transaction that resulted in the disposition of the applicable Principal Subsidiary Bank, Downey will not be required to invest the proceeds of such disposition as would otherwise be required by this paragraph (e) so long as Downey only issues Preferred Stock in such subsequent acquisition in an amount needed to replace any Preferred Stock of the acquired person outstanding at the time of, and not issued in contemplation of or in connection with, such acquisition; or

(f) any sale or issuance by any Principal Subsidiary Bank to its shareholders of additional shares of Voting Stock of, or any additional securities convertible into or exchangeable for or any additional options, warrants or rights to subscribe for or purchase shares of Voting Stock of, such Principal Subsidiary Bank at any price so long as (x) immediately prior to such sale or issuance, as the case may be, Downey owns, directly or indirectly, shares, securities, options, warrants and rights, as the case may

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be, of such Principal Subsidiary Bank of the same class or series, as the case may be, as are being sold or issued, as the case may be, and, immediately after such sale or issuance, as the case may be, Downey owns, directly or indirectly, at least as great a percentage of such class or series, as the case may be, of shares, securities, options, warrants or rights, as the case may be, of such Principal Subsidiary Bank as Downey owned immediately before such sale or issuance, as the case may be, and (y) immediately after such sale or issuance, as the case may be, and assuming the conversion or exchange, as the case may be, of all securities convertible into or exchangeable for and the exercise of any options, warrants or rights to subscribe for or purchase shares of Voting Stock of the applicable Principal Subsidiary Bank and all other Subsidiaries, Downey would own, directly or indirectly, not less than 80% of the outstanding shares of each class and series of Voting Stock of such Principal Subsidiary Bank; or

(g) any sale, assignment, transfer or other disposition of such Voting Stock or other securities made by Downey or any Subsidiary acting in a fiduciary capacity for any person other than Downey or any of its Subsidiaries.

The creation of a Lien shall not be deemed a sale, lease, assignment, transfer or other conveyance or disposition of Voting Stock, other securities or assets or property for purposes of any of the limitations described under Limitation on Sale or Issuance of Voting Stock of a Principal Subsidiary Bank above. The creation of any Liens on such Voting Stock or other securities is governed by the provisions described below under Limitations on Liens .

Limitation on Liens. Downey will not, and will not cause or permit any Subsidiary to, directly or indirectly, create, assume, incur or suffer to exist any Lien upon any shares of Voting Stock of any Principal Subsidiary Bank or any Subsidiary that owns, directly or through one or more other Subsidiaries, shares of Voting Stock of any Principal Subsidiary Bank.

The provisions set forth in the immediately preceding paragraph shall not prohibit the following:

(1) any Lien on any Voting Stock of any Principal Subsidiary Bank or any Subsidiary that owns, directly or through one or more Subsidiaries, shares of Voting Stock of any Principal Subsidiary Bank and which Lien secures loans, advances, lines of credit and other extensions of credit, provided that, so long as such Lien is in existence, Downey owns, directly or indirectly, not less than 80% of the outstanding shares of each class and series of Voting Stock of such Principal Subsidiary Bank or such other Subsidiary, as the case may be, free and clear of any Liens, other than any Liens permitted pursuant to clauses (2) through (7) below; or

(2) Liens on any shares of Voting Stock existing at the time of acquisition thereof (whether by merger, acquisition of stock or assets or otherwise) by Downey or any of its Subsidiaries, provided that such Liens were not created in contemplation of or in connection with such acquisition; or

(3) Liens securing any judgment if such judgment shall not have remained undischarged, or unstayed on appeal, for more than 60 days; or

(4) Liens for taxes, governmental assessments or similar governmental charges or levies not yet due or which are not overdue for a period of more than 30 days or which are being contested by Downey in good faith by appropriate proceedings; or

(5) Liens on Voting Stock that secure Debt owing by Downey or any Subsidiary to Downey or any Wholly-Owned Subsidiary; or

(6) any agreement to sell, assign, transfer or otherwise dispose of or issue Voting Stock or any agreement to merge or consolidate a Principal Subsidiary Bank so long as (x) such agreement does not constitute or create a mortgage, pledge, charge, security interest or similar encumbrance on any shares of Voting Stock of a Principal Subsidiary Bank or any Subsidiary that owns, directly or through one or more Subsidiaries, shares of Voting Stock of any Principal Subsidiary Bank and no such Voting Stock shall, as a result of, pursuant to or in connection with such agreement or any transaction pursuant to such agreement, serve as collateral or security for any Debt or other obligation, (y) the only Lien on shares of Voting Stock of any Principal Subsidiary Bank or any Subsidiary that owns, directly or through one or

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more other Subsidiaries, shares of Voting Stock of any Principal Subsidiary Bank created pursuant to such agreement is the agreement to sell, assign, transfer or otherwise dispose of or issue such Voting Stock or the agreement to merge or consolidate such Principal Subsidiary Bank, as the case may be, and (z) such sale, assignment, transfer, disposition, issuance, merger or consolidation, as the case may be, and such agreement comply with the covenant set forth above under Limitation on Sale or Issuance of Voting Stock of a Principal Subsidiary Bank; or

(7) Liens for the sole purpose of extending, renewing or replacing in whole or in part the Debt or other obligation secured thereby referred to in the foregoing clause (2) or in this clause (7); provided, however, that the Lien excluded pursuant to this clause (7) shall be excluded only so long as the amount of the Debt or other obligation secured thereby does not exceed the amount of the Debt or other obligation so secured at the time of such extension, renewal or replacement (together with any premium, fees or expenses (other than interest) payable in connection with any such replacement, extension or renewal), and that such extension, renewal or replacement shall be limited to all or part of the shares of Voting Stock subject to the Lien so extended, renewed or replaced.

The information appearing above under Limitation on Sale or Issuance of Voting Stock of a Principal Subsidiary Bank, and the definition of Principal Subsidiary Bank appearing below under Certain Definitions supersede and replace the information appearing under the caption Description of Senior and Subordinated Debt Securities Sale or Issuance of Capital Stock of Principal Subsidiary Bank in the accompanying prospectus.

Merger, Consolidation and Transfer of Assets

The Indenture provides that Downey will not consolidate or merge with or into any other person or sell, lease, assign, transfer or otherwise convey all or substantially all of its properties and assets to any other person unless:

either (1) Downey shall be the continuing person (in the case of a merger) or (2) the successor person (if other than Downey) formed by or resulting from the consolidation or merger or to which such assets shall have been sold, leased, assigned, transferred or otherwise conveyed is a corporation organized and existing under the laws of the United States of America or any state thereof and shall expressly assume the due and punctual payment of the principal of, premium, if any, and interest on, all of the debt securities outstanding under the Indenture and the due and punctual performance of all of Downey's other obligations under the Indenture and the debt securities outstanding thereunder by means of a supplemental indenture, satisfactory to the trustee, executed and delivered by the trustee and such successor corporation;

immediately after giving effect to such transaction or transactions, no event of default under the Indenture, and no event which, after notice or lapse of time or both would become an event of default under the Indenture, shall have occurred and be continuing; and

the trustee shall have received the officer's certificates and opinion of counsel called for by the Indenture.

Upon any consolidation by Downey with, or merger of Downey into, any other person or any sale, assignment, transfer, lease or conveyance of all or substantially all of Downey's properties and assets to any person in accordance with the provisions of the Indenture described above, the successor person formed by the consolidation or into which Downey is merged or to which the sale, assignment, transfer, lease or other conveyance is made shall succeed to, and be substituted for, Downey and may exercise every right and power of Downey under the Indenture with the same effect as if such successor person had been named as Downey therein; and thereafter, except in the case of the lease, the predecessor person shall be released from all obligations and covenants under the Indenture and the debt securities issued under the Indenture.

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Events of Default

The Indenture defines an event of default with respect to the notes as any of the following events:

(1) default in the payment of any principal of or premium, if any, on any of the notes when due; or

(2) default in the payment of any interest on any of the notes when due and continuance of that default for 30 days; or

(3) default in the performance, or breach, of any other covenant of Downey in the Indenture (other than a covenant which has expressly been included in the Indenture, whether or not by means of a supplemental indenture, solely for the benefit of debt securities of a series other than the notes), and continuance of such default or breach (without such default or breach having been waived in accordance of the provisions of the Indenture) for a period of 60 days after written notice to Downey by the trustee or to Downey and the trustee by the holders of at least 25% in aggregate principal amount of the notes then outstanding; or

(4) default under any bond, note, debenture, mortgage, indenture or other instrument under which there may be issued or by which there may be secured or evidenced any Debt of Downey or any Principal Subsidiary Bank or Significant Subsidiary, which default shall result in such Debt in an aggregate principal amount exceeding \$20 million becoming or being declared due and payable prior to the date on which it would otherwise have become due and payable, without such Debt having been discharged, or such acceleration having been rescinded or annulled, within a period of 30 days after written notice to Downey by the trustee or to Downey and the trustee by the holders of at least 25% in aggregate principal amount of the notes then outstanding; or

(5) certain instances of bankruptcy, insolvency or reorganization with respect to Downey or any Principal Subsidiary Bank or Significant Subsidiary.

If an event of default occurs with respect to the notes and is continuing, either the trustee or the holders of at least 25% in principal amount of the notes then outstanding may declare the principal of, and accrued and unpaid interest on, the notes to be due and payable immediately. Upon satisfaction by Downey of certain conditions specified in the Indenture, the holders of a majority in principal amount of the notes then outstanding may rescind and annul such declaration of an event of default and its consequences. The information set forth in this paragraph and the immediately preceding paragraph supercedes and replaces the information set forth in the accompanying prospectus in the first and third paragraphs under the caption Description of Senior and Subordinated Debt Securities Defaults and Rights of Acceleration.

The Indenture provides that, within 90 days after the occurrence of any default with respect to the notes, the trustee will mail to all holders of the notes notice of the default if known to the trustee, unless that default has been cured or waived. However, the Indenture provides that, except in the case of a default in the payment of the principal of, premium, if any, or interest on any notes, the trustee may withhold notice of a default with respect to the notes if its board of directors or executive committee or a trust committee composed of directors and/or Responsible Officers of the trustee in good faith determines that the withholding of such notice is in the interests of the holders of notes. As used in this paragraph, the term default means any event which is, or after notice or lapse of time or both would become, an event of default with respect to the notes.

Subject to the provisions of the Trust Indenture Act of 1939 requiring the trustee, during the continuance of an event of default under the Indenture, to act with the requisite standard of care, the trustee is under no obligation to exercise any of its rights or powers under the Indenture at the request or direction of any of the holders of notes unless those holders have offered the trustee security or indemnity satisfactory to the trustee. Subject to the foregoing, the holders of a majority in principal amount of the outstanding notes have the right to direct the time, method and place of conducting any proceeding for any remedy available to the trustee under the Indenture with respect to the notes. The Indenture requires the annual filing by us with the trustee of a certificate which states whether or not we are in compliance with all conditions and covenants under the Indenture. The foregoing provisions of this paragraph supercede and replace the provisions set forth in the second and third paragraphs under the caption Description of the Senior and Subordinated Debt Securities Collection of Indebtedness in the accompanying prospectus.

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Notwithstanding any other provision of the Indenture, the holder of a note will have the right, which is absolute and unconditional, to receive payment of the principal of and premium, if any, and interest on that note on the respective due dates for those payments and to institute suit for the enforcement of those payments, and this right shall not be impaired without the consent of the holder.

Certain Definitions

As used in the Indenture, the following terms have the meaning specified below:

Bank means any person which is a savings association, savings bank, savings and loan association, bank, trust company or similar entity organized and doing business under the laws of the United States of America, any State thereof or the District of Columbia.

Business Day and **business day** mean any day other than a Saturday, Sunday or other day on which banking institutions in The City of New York are authorized or obligated by law, regulation or executive order to close; provided that such term shall mean, when used with respect to any payment of principal of, or premium or interest, if any, on, the debt securities of any series to be made in a Place of Payment (which Place of Payment shall be specified in the form of such debt security or pursuant to the Indenture) other than The City of New York, any day other than a Saturday, Sunday or other day on which banking institutions in such Place of Payment are authorized or obligated by law, regulation or executive order to close. The foregoing definition supersedes and replaces the definition of **Business Day** appearing under the caption **Description of the Senior and Subordinated Debt Securities Payment of Interest** in the accompanying prospectus.

Capital Stock means, with respect to any person, any and all shares, interests, participations or other equivalents (however designated) in the equity of such person (including, without limitation, (a) with respect to a corporation, common stock, preferred stock and any other capital stock, (b) with respect to a partnership, partnership interests (whether general or limited), and (c) with respect to a limited liability company, limited liability company interests).

Common Stock means, with respect to any person, Capital Stock of such person of any class or series which has no preference or priority in respect of the payment of dividends or distributions of assets upon any voluntary or involuntary liquidation, dissolution or winding up of such person and which is not subject to redemption by such person.

Debt means indebtedness for borrowed money.

GAAP and **generally accepted accounting principles** means such accounting principles as are generally accepted in the United States of America as of the date or time of any computation required under the Indenture.

Lien means any mortgage, pledge, lien, charge, security interest, conditional sale or other title retention agreement or other encumbrances of any nature whatsoever.

Preferred Stock means, with respect to any person, any Capital Stock of such person of any class or series that ranks, in respect of the payment of dividends or distributions of assets upon any voluntary or involuntary liquidation, dissolution or winding up of such person, senior to the Common Stock of any class or series of such person.

Principal Subsidiary Bank means, as of any date, any Subsidiary Bank, any Surviving Person and any Successor Subsidiary, in any such case the total consolidated assets of which exceed 20% of the total consolidated assets of Downey and its Subsidiaries, all determined in accordance with generally accepted accounting principles as of the date of the then most recent consolidated balance sheet of Downey and its Subsidiaries. The foregoing definition supersedes and replaces the definition of **Principal Subsidiary Bank** appearing in the second paragraph under the caption **Description of the Senior and Subordinated Debt Securities Sale or Issuance of Capital Stock of Principal Subsidiary Bank** in the accompanying prospectus. As of the date of this prospectus supplement, the Bank is our only Principal Subsidiary Bank.

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Significant Subsidiary means any Subsidiary which is a significant subsidiary as defined in Rule 1-02 of Regulation S-X promulgated by the Securities and Exchange Commission, as such Rule is in effect on the date of this prospectus supplement but substituting 20 percent for 10 percent wherever a reference to 10 percent appears in such definition.

Subsidiary means (1) any corporation at least a majority of the total voting power of whose outstanding Voting Stock is owned, directly or indirectly, at the date of determination by Downey and/or one or more other Subsidiaries, and (2) any other person in which Downey and/or one or more other Subsidiaries, directly or indirectly, at the date of determination, (x) own at least a majority of the outstanding ownership interests or (y) have the power to elect or direct the election of, or to appoint or approve the appointment of, at least a majority of the directors, trustees or managing members of, or other persons holding similar positions with, such person.

Subsidiary Bank means any Subsidiary which is a Bank.

Successor Subsidiary has the meaning given to that term under Certain Covenants Limitation on Sale or Issuance of Voting Stock of a Principal Subsidiary Bank.

Surviving Person has the meaning given to that term under Certain Covenants Limitation on Sale or Issuance of Voting Stock of a Principal Subsidiary Bank.

Voting Stock means, with respect to any person, any class or series of Capital Stock of such person the holders of which are ordinarily, in the absence of contingencies, entitled to vote for the election of, or to appoint or to approve the appointment of, the directors, trustees or managing members of, or other persons holding similar positions with, such person.

Wholly-Owned Subsidiary means any Subsidiary all of whose outstanding shares of Capital Stock (other than directors qualifying shares) are owned, directly or indirectly, by Downey.

Certificated Notes

So long as the depository or its nominee is the registered owner of a global note, the depository or its nominee, as the case may be, will be considered the sole holder of the notes represented thereby for all purposes under the Indenture, including for purposes of receiving payments of principal, premium, if any, and interest.

Owners of beneficial interests in the global notes will not be considered holders of the notes under the Indenture. Accordingly, each owner of a beneficial interest in a global note must rely on the procedures of the depository and, if that beneficial owner is not a participant in the depository, on the procedures of the participant through which that beneficial owner owns its interest, in order to exercise any rights of a holder under the Indenture.

As described above, beneficial interests in the global notes generally may not be exchanged for certificated notes. However, the Indenture provides that if:

the depository for the global notes notifies us that it is unwilling or unable to continue as depository for the global notes or we become aware that the depository has ceased to be a clearing agency registered under the Securities Exchange Act of 1934 and, in any such case, we fail to appoint a successor depository within 60 calendar days;

we, in our sole discretion, determine that the global notes will be exchangeable for certificated notes; or

an event of default with respect to the notes has occurred and is continuing,

we will execute and the trustee will authenticate and deliver certificated notes in exchange for interests in the global notes. We anticipate that those certificated notes will be registered in such name or names as the depository instructs the trustee and that those instructions will be based upon directions received by the depository from its participants with respect to ownership of beneficial interests in the global notes. The

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information in this paragraph supercedes and replaces the information set forth in the seventh paragraph under the caption Book-Entry Issuance in the accompanying prospectus.

We obtained the information in this section and elsewhere in the accompanying prospectus concerning DTC and DTC's book-entry system from sources that we believe to be reliable, but we take no responsibility for the accuracy of that information.

Modification and Waivers

The Indenture permits us and the trustee, with the consent of the holders of a majority in principal amount of the outstanding debt securities of each series issued under the Indenture and affected by such modification or amendment, to modify or amend any of the provisions of the Indenture or of the debt securities of the applicable series or the rights of the holders of the debt securities of that series under the Indenture. However, no such modification or amendment shall, among other things:

change the stated maturity of the principal of, or premium, if any, or any installment of interest, if any, on any debt securities;

reduce the principal of or any premium on any debt securities or reduce the rate of interest on or the redemption or repurchase price of any debt security;

reduce the amount of principal of any original issue discount security that would be due and payable upon an acceleration of the maturity of such debt security;

adversely affect any right of repayment or repurchase at the option of any holder;

change any place where or the currency in which debt securities are payable;

impair the holder's right to institute legal proceedings to enforce the payment of any principal of or premium or interest, if any, on any debt securities on or after the date on which such payment is due or, in the case of any debt security which is convertible into or exchangeable for other securities, to enforce the right to convert or exchange that debt security in accordance with its terms;

make any change that adversely affects the right, if any, to convert or exchange debt securities for other securities or property;

reduce the percentage of debt securities of any series whose holders must consent to any modification or amendment or any waiver of compliance with specific provisions of the Indenture or specified defaults under the Indenture and their consequences; or

reduce the requirements for a quorum or voting at a meeting of holders of the debt securities of any series, without in each case obtaining the consent of the holder of each outstanding debt security issued under the Indenture affected by the modification or amendment.

The Indenture also contains provisions permitting us and the trustee, without the consent of the holders of any debt securities issued under the Indenture, to modify or amend the Indenture, among other things:

to evidence the succession of another person to us under the Indenture and the assumption by that successor of our covenants contained in the Indenture and the debt securities;

to add to our covenants for the benefit of the holders of all or any series of debt securities issued under the Indenture;

to cure any ambiguity or correct or supplement any provision in the Indenture which may be defective or inconsistent with other provisions in the Indenture, or to make any other provisions with respect to matters or questions arising under the Indenture which shall not adversely affect the interests of the holders of the debt securities;

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to change or eliminate any provision contained in the Indenture, provided that the change (1) shall become effective only when there is no outstanding debt security of any series created prior to the execution of the applicable supplemental indenture that is entitled to the benefit of that provision or (2) shall not adversely affect any debt security outstanding; and

to establish the form or terms of debt securities of any series.

The holders of a majority in aggregate principal amount of the outstanding debt securities of any series may waive our compliance with some of the restrictive provisions of the Indenture, including the covenants described above under Certain Covenants. The holders of a majority in aggregate principal amount of the outstanding debt securities of any series may, on behalf of all holders of debt securities of that series, waive any past default under the Indenture with respect to debt securities of that series and its consequences, except a default in the payment of the principal of, or premium, if any, or interest, if any, on debt securities of that series or, in the case of any debt securities which are convertible into or exchangeable for other securities, a default in any such conversion or exchange, or a default in respect of a covenant or provision which cannot be modified or amended without the consent of the holder of each outstanding debt security of the affected series.

The provisions described under this caption Modification and Waivers supercede and replace the provisions described under Description of the Senior and Subordinated Debt Securities Waiver of Covenants and Description of Senior and Subordinated Debt Securities Modification of the Indentures in the accompanying prospectus.

Meetings by Noteholders

The trustee may call a meeting of the holders of the debt securities of any series in its discretion or upon request by us or the holders of at least 10% in principal amount of the outstanding debt securities of that series. If a meeting of holders of debt securities of any series is held, any resolution adopted or decision taken will be binding on all holders of debt securities of that series outstanding under the Indenture. The information in this paragraph supersedes and replaces the information under the caption Description of Senior and Subordinated Debt Securities Meetings and Actions by Noteholders in the accompanying prospectus.

Satisfaction and Discharge

If at any time:

(1) Downey has delivered to the trustee for cancellation, subject to specified exceptions, all notes issued under the Indenture, or

(2) all notes not previously delivered to the trustee for cancellation have become due and payable, or are by their terms to become due and payable within one year or are to be called for redemption within one year under arrangements satisfactory to the trustee for the giving of notice of redemption, and Downey has deposited with the trustee as trust funds an amount sufficient to pay at maturity or upon redemption the principal of, premium, if any, and interest on the notes to the date of maturity or redemption date, as the case may be, and if Downey has satisfied other specified conditions under the Indenture, then the Indenture will cease to be of further effect with respect to the notes, except for certain provisions of the Indenture that will survive such satisfaction and discharge.

Defeasance; Covenant Defeasance

At Downey's option, either (a) Downey will be deemed to have paid and discharged all of the outstanding notes (defeasance) or (b) Downey will cease to have any obligation to comply with the

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covenants described under Certain Covenants and any failure to comply with these covenants will not constitute an event of default with respect to the notes (covenant defeasance), when:

either:

(a) Downey has deposited with the trustee in trust an amount sufficient to pay the principal of, premium, if any, and interest on the notes to the date of their stated maturity or any redemption date or Downey has deposited with the trustee in trust such amount of Government Obligations, maturing as to principal and interest in such amounts and at such times as will be sufficient to pay and discharge the principal, premium, if any, and interest on the notes to the stated maturity date or redemption date, as the case may be; or

(b) Downey has effected satisfaction and discharge of the notes as described above under Satisfaction and Discharge, including, without limitation, by depositing with the trustee the amount referred to in subparagraph (2) under such caption;

in the case of defeasance, Downey has delivered to the trustee an opinion of counsel stating that (a) Downey has received from, or there has been published by, the Internal Revenue Service, a ruling or (b) since the date of execution of the Indenture (meaning the date of execution of the original Indenture and not any supplemental indentures thereto), there has been a change in applicable federal income tax law, in either case to the effect that, and based thereon that opinion will confirm that, the holders of the outstanding notes will not recognize income, gain or loss for federal income tax purposes as a result of such deposit, defeasance and discharge and will be subject to federal income tax on the same amounts, in the same manner and at the same times as would have been the case if such deposit, defeasance and discharge had not occurred;

in the case of covenant defeasance, Downey has delivered to the trustee an opinion of counsel stating that the holders of the outstanding notes will not recognize income, gain or loss for federal income tax purposes as a result of such deposit and covenant defeasance and will be subject to federal income tax on the same amounts, in the same manner and at the same times as would have been the case if such deposit and covenant defeasance had not occurred;

Downey has paid or caused to be paid all other sums payable with respect to the notes;

such defeasance or covenant defeasance, as the case may be, shall not result in a breach of violation of, or constitute a default under, the Indenture or any other material agreement or instrument to which Downey is a party;

no event of default with respect to the notes or event which, with notice or lapse of time or both, would become an event of default with respect to the notes shall have occurred and be continuing on the date of the deposit referred to in subparagraph (a) or (b) in the first bullet point above, as the case may be, and, in the case of defeasance, no event of default with respect to notes arising from specified events of bankruptcy, insolvency or reorganization with respect to Downey and no event which, with notice or lapse of time or both, would become such an event of default with respect to the notes shall have occurred and be continuing at any time during the period through and including the 91st day after the date of such deposit; and

Downey has satisfied certain other conditions specified in the Indenture.

If any outstanding notes are to be redeemed prior to their stated maturity in connection with any such defeasance or covenant defeasance, Downey is required by the Indenture to make arrangements satisfactory to the trustee for the giving of notice of redemption.

In the event that Downey effects covenant defeasance with respect to the notes and the notes are declared due and payable prior to maturity because of the occurrence of any event of default other than an event of default with respect to the covenants as to which covenant defeasance has been effected (which covenants would no longer be applicable to the notes), the amount of moneys or Government Obligations deposited with the Trustee to effect covenant defeasance may not be sufficient to pay amounts due on the notes at the time of

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any acceleration resulting from the event of default. However, Downey would remain liable to make payments of those amounts.

Applicable Law

The notes and the Indenture will be governed by and construed in accordance with the laws of the State of New York.

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CERTAIN UNITED STATES FEDERAL INCOME TAX CONSIDERATIONS

General

In this section, we summarize certain of the material United States federal income tax consequences of purchasing, holding and selling the notes. This summary provides general information only and is directed solely to beneficial owners purchasing notes at the issue price, that is, the first price to the public at which a substantial amount of the notes is sold (excluding sales to bond houses, brokers or similar persons or organizations acting in the capacity of underwriters, placement agents or wholesalers). Except where we state otherwise, this summary deals only with notes held as capital assets (as defined in the Internal Revenue Code of 1986, as amended (the Code)), by a U.S. Holder (as defined below) who purchases the notes at their original offering price when we originally issue them.

We do not address all of the tax consequences that may be relevant to a U.S. Holder. We also do not address, except as stated below, any of the tax consequences to holders that are Non-U.S. Holders (as defined below) or to holders that may be subject to special tax treatment, including banks, thrift institutions, real estate investment trusts, personal holding companies, insurance companies, and brokers and dealers in securities or currencies. Further, we do not address:

the United States federal income tax consequences to stockholders in, or partners or beneficiaries of, an entity that is a holder of the notes;

the United States federal estate and gift or alternative minimum tax consequences of the purchase, ownership or sale of the notes;

persons who hold the notes in a straddle or as part of a hedging, conversion or constructive sale transaction or whose functional currency is not the United States dollar; or

any state, local or foreign tax consequences of the purchase, ownership and sale of notes.

Accordingly, you should consult your tax advisor regarding the tax consequences of purchasing, owning and selling the notes in light of your circumstances.

A U.S. Holder is a beneficial owner of a note that is for United States federal income tax purposes:

a citizen or resident of the United States;

a corporation or partnership (or other entity treated as a corporation or partnership for federal income tax purposes) created or organized in or under the laws of the United States, any state thereof or the District of Columbia (unless in the case of a partnership, Treasury regulations provide otherwise);

an estate if its income is subject to United States federal income taxation regardless of its source; or

a trust if (1) a United States court can exercise primary supervision over its administration and (2) one or more United States persons have the authority to control all of its substantial decisions.

A Non-U.S. Holder is a noteholder other than a U.S. Holder.

This summary is based on the Code, Treasury regulations issued under the Code, and administrative judicial interpretations thereof, all as they currently exist as of the date of this prospectus supplement and all of which are subject to change (possibly with retroactive effect).

Interest

We expect that the notes will not be issued with more than a *de minimis* amount of original issue discount, if any. Therefore, interest on a note generally will be taxable to a U.S. Holder as ordinary income as it accrues or is received in accordance with the U.S. Holder's method of accounting for United States federal income tax purposes.

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Sales or Redemption of Notes

If a U.S. Holder sells notes or if the notes are redeemed, the U.S. Holder will recognize gain or loss in an amount equal to the difference between the adjusted tax basis in the notes and the amount realized from the sale or redemption (generally, the U.S. Holder's selling price or the redemption price less any amount received in respect of accrued but unpaid interest not previously included in the U.S. Holder's income). A U.S. Holder's adjusted tax basis in the notes generally will equal the U.S. Holder's cost of the notes. Gain or loss on the sale of notes generally will be a capital gain or loss. Any amounts attributable to interest in the case of a redemption of the notes will be ordinary interest income.

Information Reporting

Generally, income on the notes will be reported to a noteholder on an Internal Revenue Service Form 1099, which should be mailed by January 31 following each calendar year.

Non-U.S. Holders

Payments to a Non-U.S. Holder that are not effectively connected with the conduct of a U.S. trade or business will generally not be subject to United States federal withholding tax, provided the Non-U.S. Holder:

does not own (directly or indirectly, actually or constructively) 10% or more of the total combined voting power of all classes of our stock entitled to vote;

is not a controlled foreign corporation that is related to us through stock ownership; and

is not a bank receiving interest described in section 881(c)(3)(A) of the Code.

To qualify for this exemption from withholding, the last United States payor in the chain of payment prior to payment to a Non-U.S. Holder (the withholding agent) must have received a statement that provides the name and address of the Non-U.S. Holder.

The statement may be made on an Internal Revenue Service Form W-8BEN or a substantially similar form, which is generally valid for the year of signature plus three additional years. Notwithstanding the above, a holder must inform the withholding agent of any change in the information on the statement within 30 days of any change. If the notes are held through a securities clearing organization or certain other financial institutions that are not qualified intermediaries, the organization or institution may provide a signed statement to the withholding agent along with a copy of Internal Revenue Service Form W-8BEN or the substitute form provided by the Non-U.S. Holder. A Non-U.S. Holder who is not an individual or a corporation (or an entity treated as a corporation for federal income tax purposes) holding the notes on its own behalf may have substantially increased reporting requirements. In particular, in the case of notes held by a foreign partnership (or foreign trust), the partners (or beneficiaries) rather than the partnership (or trust) will be required to provide the certification discussed above, and the partnership (or trust) will be required to provide certain additional information.

A Non-U.S. Holder will generally not be subject to United States federal withholding or income tax on any gain realized upon the sale or other disposition of the notes. If, however, a Non-U.S. Holder holds the notes in connection with a trade or business conducted in the United States or is present in the United States for 183 days or more during the taxable year of disposition or redemption and certain other conditions are met, it may be subject to income tax on all income and gains recognized.

Backup Withholding

Backup withholding at the applicable statutory rate of United States federal income tax may apply to payments made with respect to the notes to registered owners who are not exempt recipients and who fail to provide certain identifying information (such as the registered owner's taxpayer identification number) in the required manner, under-report their tax liability or otherwise fail to comply with applicable United States information reporting or certification requirements. Generally, individuals are not exempt recipients, whereas corporations and certain other entities generally are exempt recipients. Payments made with respect to the

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notes to a U.S. Holder must be reported, unless the U.S. Holder is an exempt recipient or establishes an exemption. Compliance with the identification procedures described in the preceding section would establish an exemption from backup withholding for those Non-U.S. Holders who are not exempt recipients.

Any amounts withheld under the backup withholding rules from a payment to a beneficial owner would be allowed as a refund or a credit against such beneficial owner's United States federal income tax provided the required information is furnished by the beneficial owner.

Prospective investors should consult their own tax advisors concerning the tax consequences of their particular situations.

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WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission, or SEC. You may read and copy any document which Downey files at the SEC's public reference rooms in Washington, D.C., Chicago, Illinois and New York, New York. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. Our filings with the SEC are also available to the public over the Internet at a World Wide Web site maintained by the SEC at <http://www.sec.gov> and on our website <http://www.downeysavings.com>. Information on our website does not constitute a part of this prospectus supplement or the accompanying prospectus. In addition, you may inspect our reports, proxy statements and other information at the offices of the New York Stock Exchange.

On November 21, 2000, Downey filed with the SEC a Registration Statement on Form S-3 under the Securities Act of 1933 with respect to the securities offered by this prospectus supplement and accompanying prospectus. This prospectus supplement and accompanying prospectus do not contain all of the information shown in the Registration Statement. For further information with respect to Downey and the securities offered by this prospectus supplement and accompanying prospectus, reference is made to the Registration Statement and the exhibits thereto which you may inspect at the public reference facilities of the SEC or through the SEC's website.

DOCUMENTS INCORPORATED BY REFERENCE

The SEC allows us to incorporate by reference information into this supplemental prospectus and accompanying prospectus, which means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be a part of this prospectus supplement and accompanying prospectus, and information that we file later with the SEC will automatically update and supersede this information. We incorporate by reference the documents listed below and any future filings made by us with the SEC which we may make under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 until we sell all of the securities offered hereby:

our Annual Report on Form 10-K for the year ended December 31, 2003;

our Quarterly Report on Form 10-Q for the quarter ended March 31, 2004; and

our Current Reports on Form 8-K dated January 23, 2004, March 23, 2004, and April 19, 2004.

Notwithstanding the foregoing and notwithstanding anything to the contrary appearing in the accompanying prospectus, any document or portion of a document that is furnished to the SEC and is not deemed to be filed with the SEC under the Securities Exchange Act shall not be incorporated or deemed to be incorporated by reference in this prospectus supplement or the accompanying prospectus.

You may request a copy of these incorporated filings, without charge, excluding all exhibits unless specifically incorporated by reference as an exhibit to this prospectus supplement and accompanying prospectus, as well as copies of the form of Indenture and the form of certificate evidencing the notes. You may request copies by writing or telephoning Downey Financial Corp., 3501 Jamboree Road, Newport Beach, California 92660, Attention: Corporate Secretary, telephone (949) 854-0300.

Table of Contents**UNDERWRITING**

Subject to the terms and conditions set forth in the underwriting agreement dated the date of this prospectus supplement, each of the underwriters named below, for whom Credit Suisse First Boston LLC and J.P. Morgan Securities Inc., are acting as joint book-running managers, has severally agreed to purchase, and we have agreed to sell to each underwriter, the principal amount of notes set forth opposite the name of each underwriter:

Underwriters	Principal Amount
Credit Suisse First Boston LLC	\$
J.P. Morgan Securities Inc.	
Friedman, Billings, Ramsey & Co., Inc.	
NBC Capital Markets Group, Inc.	
Fox-Pitt, Kelton Inc.	
	—
Total	\$

Under the terms and conditions of the underwriting agreement, if the underwriters take any of the notes, then they are obligated to take and pay for all of the notes. The underwriting agreement provides that, if an underwriter defaults on its obligation to purchase notes, the purchase commitments of the non-defaulting underwriters may be increased or the offering of the notes terminated.

The notes are a new issue of securities with no established trading market and will not be listed on any national securities exchange or included for quotation on any automated quotation system. The underwriters have advised us that they intend to make a market in the notes, but they have no obligation to do so and may discontinue market making at any time without providing any notice. No assurance can be given that a trading market for the notes will develop or as to the liquidity of any trading market for the notes that may develop.

The underwriters initially propose to offer part of the notes directly to the public at the offering price described on the cover page of this prospectus supplement and part to certain dealers at a price that represents a concession not in excess of % of the principal amount of the notes. The underwriters may allow, and any such dealer may realow, a concession not in excess of % of the principal amount of the notes to certain other dealers. After the initial offering of the notes, the underwriters may from time to time vary the offering price and other selling terms.

We have also agreed to indemnify the underwriters against certain liabilities, including liabilities under the Securities Act of 1933, as amended, or to contribute to payments which the underwriters may be required to make in respect of any such liabilities.

In connection with the offering of the notes, the underwriters may engage in transactions that stabilize, maintain or otherwise affect the price of the notes. Specifically, the underwriters may over allot in connection with the offering of the notes, creating a short position. In addition, the underwriters may bid for, and purchase, notes in the open market to cover short positions or to stabilize the price of the notes. Finally, the underwriting syndicate may reclaim selling concessions allowed for distributing the notes in this offering, if the syndicate repurchases previously distributed notes in syndicate covering transactions, stabilization transactions or otherwise. Any of these activities may stabilize or maintain the market price of the notes above independent market levels. The underwriters are not required to engage in any of these activities, and may end any of them at any time.

Our expenses (excluding underwriting discounts) associated with this offering, to be paid by us, are estimated to be \$.

Credit Suisse First Boston LLC, or CSFB, and J.P. Morgan Securities Inc., or JPMorgan, will make the notes available for distribution on the Internet through a proprietary web site and/or a third-party system operated by MarketAxess Corporation, an Internet-based communications technology provider. MarketAxess Corporation is providing the system as a conduit for communications between CSFB and JPMorgan and their

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respective customers and is not a party to any transactions. MarketAxess Corporation, a registered broker-dealer, will receive compensation from CSFB and JPMorgan based on transactions CSFB and JPMorgan, respectively, conduct through the system. CSFB and JPMorgan will make the notes available to their respective customers through the Internet distributions, whether made through a proprietary or third-party system, on the same terms as distributions made through other channels.

In the ordinary course of their respective businesses, certain of the underwriters or their affiliates have engaged, and may in the future engage, in commercial banking and/or investment banking transactions with us and our affiliates for which they have received and may in the future receive compensation.

We expect to deliver the notes against payment for the notes on or about the date specified in the last paragraph of the cover page of this prospectus supplement, which will be the fifth business day following the date of this prospectus supplement. Under Rule 15c6-1 of the Securities Exchange Act of 1934, trades in the secondary market generally are required to settle in three business days, unless the parties to a trade expressly agree otherwise. Accordingly, purchasers who wish to trade notes on the date of this prospectus supplement or the next succeeding business day will be required, by virtue of the fact that the notes initially will settle in T+5, to specify alternative settlement arrangements to prevent a failed settlement.

LEGAL MATTERS

Certain legal matters with respect to the notes will be passed upon by Manatt, Phelps & Phillips, LLP, Los Angeles, California, counsel to Downey, Sidley Austin Brown & Wood, LLP, San Francisco, California will act as counsel for the underwriters.

EXPERTS

Our consolidated financial statements as of December 31, 2003 and 2002, and for each of the years in the three-year period ended December 31, 2003, have been incorporated by reference into this prospectus supplement in reliance upon the report of KPMG LLP, independent registered public accounting firm, which is incorporated herein by reference, and upon the authority of said firm as experts in accounting and auditing.

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PROSPECTUS

\$300,000,000

Downey Financial Corp.

May offer: Common Stock

Preferred Stock

Debt Securities

Downey Financial Capital Trust II

and

Downey Financial Capital Trust III

May offer: Capital Securities (Trust Preferred Securities)

**guaranteed, to the extent described herein,
by Downey Financial Corp.**

Downey Financial Corp. and, in the case of the capital securities, the applicable trust, will provide the specific terms of these securities in supplements to this prospectus. You should read this prospectus and the accompanying prospectus supplement carefully before you invest.

Downey Financial Corp. and the trusts may use this prospectus to offer up to \$300,000,000 of securities.

Downey Financial Capital Trusts II and III may offer capital securities that Downey Financial Corp. will fully and unconditionally guarantee, to the extent described herein, based on its obligations under a guarantee and a trust agreement for each trust and an indenture.

Downey Financial Corp. common stock is traded on the New York Stock Exchange and Pacific Exchange under the symbol DSL .

These securities are not deposits or other obligations of a bank and are not insured by the Federal Deposit Insurance Corporation or any other government agency.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

December 1, 2000

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PROSPECTUS SUMMARY

This summary provides a brief overview of aspects of Downey Financial Corp. and Downey Financial Capital Trusts II and III and some of the terms of the offered securities that are known as of the date of this prospectus. In this prospectus, Downey, we, us, and our refer to Downey Financial Corp. and its consolidated subsidiaries unless otherwise expressly stated or where the context otherwise requires and trusts refers to Downey Financial Capital Trusts II and III. For more complete information on Downey and the trusts and a more complete understanding of the terms of the offered securities, before making your investment decision, you should carefully read:

this prospectus, which explains the general terms of the securities that Downey and the trusts may offer;

the accompanying prospectus supplement, which (1) explains the specific terms of the securities being offered and (2) updates and changes information in this prospectus; and

the documents referred to in **Where You Can Find More Information** for information about Downey, including its financial statements.
Downey Financial Corp.

Downey is a California-based savings and loan holding company. Our principal subsidiary is Downey Savings and Loan Association F.A., which we refer to as the **Bank**. The Bank:

is one of the largest financial institutions headquartered in Southern California, based on total assets;

was formed in 1957 as a California-licensed savings and loan and converted to a federal charter in 1995; and

at September 30, 2000, operated through 107 retail branches, including 43 full-service in-store branches in California, and eight California loan production offices.

For the year ended December 31, 1999, we had the best year in our then 43-year history with record:

net income of \$63.8 million, or \$2.26 per share on a diluted basis, an increase of 10.1% from 1998;

asset growth of \$3.1 billion, or 50%, to \$9.4 billion; and

loan production of \$7.2 billion.

For the nine months ended September 30, 2000, we had:

net income (excluding a \$5.6 million after-tax gain from the sale of our indirect automobile finance subsidiary) of \$70.6 million, or \$2.50 per share on a diluted basis, an increase of 60.7% over the comparable 1999 period;

total assets of \$10.4 billion;

total deposits of \$7.7 billion;

total stockholders' equity of \$603 million; and

non-performing assets of only \$50 million or 0.48% of total assets.

Banking Activities

Our primary business is banking. Our banking activities focus on:

the origination of loans, primarily loans secured by single family residential properties, which are either retained in our portfolio or sold in the secondary market;

the attraction of low-cost deposits through our retail branches;

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providing exceptional customer service; and

providing innovative new products and services, including an increasing focus on products offered over the Internet and on-line banking.

The types of loans we offer include:

adjustable rate residential mortgage loans, with rates tied primarily to the Eleventh District Cost of Funds Index, including subprime loans which carry higher interest rates;

fixed rate residential mortgage loans;

commercial real estate loans, including loans secured by retail neighborhood shopping centers;

construction loans; and

consumer loans.

We also invest in various securities primarily short-term obligations to satisfy bank regulations regarding minimum levels of liquid assets.

Net income from our banking operations totaled \$53.8 million in 1999 and \$66.5 million for the first nine months of 2000 (excluding the \$5.6 million after-tax gain from the sale of our indirect automobile finance subsidiary).

Real Estate Investment Activities

Downey is also involved in real estate investment, which is conducted primarily through the Bank's subsidiary, DSL Service Company. Activities include development, construction and property management relating to our portfolio of projects primarily within California but also in Arizona. Because of regulatory restrictions that have been placed on real estate investment activities, we have reduced the amount of this business in recent years. Net income from our real estate investment and real estate joint venture activities was \$10.0 million in 1999 and \$4.2 million for the first nine months of 2000.

Operating Strategy

Our operating strategy is to:

capitalize on our strong position in our core California market and expand our Internet business;

focus on our residential lending expertise;

maintain our high lending standards and strong asset quality;

continue to strengthen our retail franchise, including the establishment of additional in-store branches;

continue to focus on attracting low cost deposits from our retail customer base;

maintain the high quality of our service to depositors and borrowers; and

improve our operating efficiency.

Our principal executive offices are located at 3501 Jamboree Road, Newport Beach, California, 92660, and our telephone number is (949) 854-0300.

Downey Financial Capital Trusts II and III

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Each of the trusts is a business trust formed under Delaware law. When we are ready to issue and sell capital securities through a trust, we will amend the trust agreements we signed in forming the trusts to read substantially like the forms of amended and restated trust agreements that have been filed with the SEC as an

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exhibit to the registration statement of which this prospectus is a part. We have established each trust solely for the following purposes:

- to issue and sell to the public its capital securities, which represent an undivided beneficial interest in the assets of the trust;
- to issue and sell its common securities to Downey in a total liquidation amount equal to at least 3% of the total capital of the trust;
- to use the proceeds from the sale of its common securities and capital securities to acquire junior subordinated debentures from Downey; and
- to engage in other activities that are directly related to the activities listed above.

Because each trust has been established only for the purposes listed above, the junior subordinated debentures will be the sole assets of the trust, and payments on the junior subordinated debentures will be the sole source of income to the trust. There are five trustees of each trust. Three of them, the administrative trustees, are officers of Downey. Unless otherwise stated in the relevant prospectus supplement, Wilmington Trust Company will act as the property trustee of the trust and will also act as the Delaware trustee of the trust.

The common securities will have terms substantially identical to and will rank equal, and payments will be made thereon pro rata, with the capital securities. However, if Downey defaults on the junior subordinated debentures, then cash distributions and liquidation, redemption and other amounts payable on the common securities will be subordinate to the capital securities in priority of payment.

Each trust has a term set forth in the prospectus supplement, but may terminate earlier if specific conditions are met. The trusts' principal offices are located at 3501 Jamboree Road, Newport Beach, California 92660, and related telephone number is (949) 854-0300.

The Securities that may be Offered

This section summarizes the legal and financial terms of the securities that are described in more detail elsewhere in this prospectus. Final terms of any particular security are set at the time of sale and are contained in the prospectus supplement relating to those securities. That prospectus supplement may vary from and supersede the terms contained in this prospectus. In addition, you should read the more detailed information appearing elsewhere in this prospectus and in the prospectus supplement. The maximum aggregate amount of securities that may be offered by Downey and the trusts is \$300,000,000. Neither Downey nor the trusts are required to offer any securities.

The Offering of Common Stock

Issuer	Downey Financial Corp.
Amount and Price	The price per share and amount are set forth in the relevant prospectus supplement and were determined by the board of directors. Downey is authorized to issue up to a total of 50,000,000 shares of common stock.
Dividends	Downey considers the payment of a quarterly dividend every quarter but is not required to pay a dividend. During 2000, a \$0.09 dividend per share was declared during each of the first three quarters.
Voting Rights	Each share is entitled to one vote at meetings of stockholders.

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The Offering of Preferred Stock

Issuer	Downey Financial Corp.
Amount and Price	The price per share and amount are set forth in the relevant prospectus supplement and were determined by the board of directors. Downey is authorized to issue up to a total of 5,000,000 shares of preferred stock.
Terms and Conditions	Downey may vary the terms of preferred stock in one or more series as set forth in the relevant prospectus supplement. The terms may differ in number of share in each series, the designation, powers preferences and rights of shares in each series and the qualifications, limitations and restrictions of each series. These terms include such things as dividend, conversion and exchange and redemption rights as well as liquidation privileges.

Voting Rights Unless otherwise provided, holders of shares of preferred stock have no voting rights except to the extent required by law.

The Offering of Senior and Subordinated Debt Securities

Issuer	Downey Financial Corp.
Amount	Downey may issue up to \$300,000,000 of notes in connection with this prospectus. There are no limitations on our ability to issue additional indebtedness.
Denominations	The notes are issued and sold usually in denominations of multiples of \$1,000.
Status	The notes are our direct obligations. Each relevant prospectus supplement states whether the notes are senior or subordinated debt. Senior notes rank equally with our other unsecured senior debt. Subordinated notes rank equally with our other unsecured subordinated debt, junior in right of payment to our senior debt, and senior in right of payment to our junior subordinated debentures.
Holders of Subordinated Notes have Limited Rights	Payment of principal of our subordinated notes may not be accelerated if there is a default in the payment of principal or any premium or interest or the performance of any of our other Indenture covenants.
Maturities	The notes are due nine months or more from the date of issue.
Interest	Each note bears interest at the specified rate or rate determined on the basis of the method set forth in the relevant prospectus supplement from the issue date; Interest on each note is payable either monthly, quarterly, semi-annually or annually on each interest payment date and on the maturity date. Interest also will be paid on the date of redemption or repayment if a note is repurchased by us prior to maturity; and

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Interest on the notes is computed on the basis of a 360-day year of twelve 30-day months, unless otherwise stated in the relevant prospectus supplement.

Principal The principal amount of the notes is payable on the maturity date at the corporate trust office of the paying agent or at any other place we may designate.

Redemption and Repayment Unless otherwise stated in the relevant prospectus supplement, the notes are not redeemable at our option or at the option of the holder, or repayable prior to the maturity date; and

The notes are unsecured and not subject to any sinking fund.

Survivor's Options Specific notes may contain a provision permitting the optional redemption of those notes prior to maturity upon the death of a purchaser holding the notes for at least six months prior to the holder's death. Your notes may not be redeemed unless that right is specified in the prospectus supplement for your notes. The right to exercise the Survivor's Option is subject to limits set by us on the permitted dollar amount of total exercises by holders of notes in any calendar year. Additional details of this right are described in the section entitled "Description of Senior and Subordinated Debt Securities Survivor's Option."

Sale and Clearance Notes are issued in book-entry only form and clear through The Depository Trust Company. Downey does not intend to issue notes in certificated form.

Trustee The trustee for senior and subordinated notes is Wilmington Trust Company, Rodney Square North, 1100 North Market Street, Wilmington, DE 19890, under separate Indentures, each dated as of November 15, 2000.

The Offering of Capital Securities, Junior Subordinated Debentures and Guarantees

Capital Securities Issuers Downey Financial Capital Trusts II and III

Junior Subordinated Debenture and Guarantees Issuer Downey Financial Corp.

Securities Offered The capital securities of the trusts represent undivided beneficial interests in the assets of the trust. Each capital security will entitle the holder to receive cumulative periodic cash distributions based on a liquidation amount set forth in the relevant prospectus supplement.

The Trusts' Assets Each trust will sell the capital securities to the public and will sell its common securities to Downey. Each trust will use the proceeds from these sales to buy a series of junior subordinated debentures from Downey. When Downey pays interest on the junior subordinated debentures, each trust will pay distributions on the capital securities at the same rate and at the same times as Downey pays interest.

Distributions On the Capital Securities Holders of capital securities will be entitled to receive cumulative cash distributions at the specified annual rate or rate determined on the basis of the method set forth in the relevant prospectus

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supplement based on the liquidation amount per capital security as set forth in the relevant prospectus supplement. Distributions will accrue from the date of original issuance, and will be paid periodically as described in the relevant prospectus supplement, unless these payments are deferred as described below. The amount of each periodic distribution will include amounts accrued to but excluding the date the distribution payment is due.

Deferral of Distributions

The payment of distributions on the capital securities may be deferred if Downey defers payments of interest on the junior subordinated debentures. Unless otherwise provided in the relevant prospectus supplement, Downey will have the right, on one or more occasions, to defer payments of interest on the junior subordinated debentures for a number of consecutive interest periods specified in the prospectus supplement.

Redemption of the Capital Securities

Each trust's duties to redeem the capital securities depend on Downey's repayment of the junior subordinated debentures. Each trust is required to redeem all of the outstanding capital securities when the junior subordinated debentures are repaid at maturity. The junior subordinated debentures are scheduled to mature as set forth in the relevant prospectus supplement.

The junior subordinated debentures will provide the terms upon which Downey can redeem the junior subordinated debentures at its option, and will specify, except with respect to specific events, a date prior to which Downey will not be allowed to redeem the junior subordinated debentures, and after which Downey will have the right to redeem the junior subordinated debentures, in whole or in part.

Except as otherwise specified in the relevant prospectus supplement, if specific special events occur relating to changes in tax or investment company laws and regulations or in the treatment of capital securities for bank regulatory purposes, Downey will have the option to redeem the junior subordinated debentures held by the trust, in whole but not in part, at any time within 90 days thereafter. These special events are more fully described under the caption "Description of the Capital Securities - Redemption."

If Downey redeems any junior subordinated debentures before their maturity, each trust will use the cash it receives on the redemption of the junior subordinated debentures to redeem, on a pro rata basis, capital securities and common securities having an aggregate liquidation amount equal to the aggregate principal amount of the junior subordinated debentures being redeemed. When a trust redeems capital securities, holders will be entitled to receive an amount set forth in the relevant prospectus supplement plus any accumulated and unpaid distributions.

Shortening of the Maturity of the Junior Subordinated Debentures

Downey will have the right to shorten the maturity of the junior subordinated debentures, unless otherwise stated in the relevant prospectus supplement.

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Capital Securities Guarantee	In connection with the issuance of the capital securities, Downey will enter into a capital securities guarantee agreement with Wilmington Trust Company, as guarantee trustee for each trust. Under that agreement, Downey will guarantee, on a subordinated basis and to the extent described in this prospectus, the payment of all amounts due on the capital securities.
Distribution of Junior Subordinated Debentures	Downey will have the right to dissolve the trusts at any time, so long as Downey obtains the prior approval of its primary federal regulator, if that approval is required under applicable law. If Downey dissolves a trust, or if a trust automatically dissolves because of other specified events, after creditor liabilities are satisfied, the trust will distribute to the holders of its capital securities and common securities, on a pro rata basis, junior subordinated debentures with a principal amount equal to the stated liquidation amount of each capital security and common security. If the property trustee determines that a distribution is impractical, then holders of capital securities and common securities will be entitled to receive, on a pro rata basis, out of assets held by the trust, so long as the rights of any creditors of the trust are already satisfied, an amount equal to the stated liquidation amount plus accrued and unpaid distributions. If the trust does not have enough assets to pay this amount to each holder of capital securities in full, liquidating distributions will be paid, first to holders of capital securities on a pro rata basis before holders of common securities will be entitled to receive any moneys.
Ranking of the Capital Securities	In general, the capital securities will rank on a parity in right of payment and payments thereon will be made pro rata with the common securities of the trust. However, the capital securities will have a preference under specific circumstances with respect to cash distributions and amounts payable on liquidation, redemption or otherwise over the common securities, which will be held by Downey.
Voting Rights of the Holders of Capital Securities	Holders of capital securities will generally have limited voting rights relating only to the modification of the capital securities, the dissolution, winding-up or termination of the trusts. For more information, see below under the caption Description of the Capital Securities Voting Rights; Amendment of the Trust Agreement.

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A WARNING ABOUT FORWARD-LOOKING INFORMATION

Downey Financial Corp. and Downey Financial Capital Trusts II and III have each made forward-looking statements in this prospectus, the accompanying prospectus supplement and in documents that are incorporated by reference in this prospectus, that are subject to risks and uncertainties. These statements are based on the beliefs and assumptions of management and on information currently available to management. Forward-looking statements include the information concerning possible or assumed future operating results and financial condition appearing in this prospectus and the accompanying prospectus supplement, in documents that are incorporated by reference in this prospectus and statements preceded by, followed by or that include the words believes, expects, anticipates, intends, plans, estimates or similar expressions. Although we believe that our expectations are based on reasonable assumptions, actual results may differ materially from our expectations. Factors that could cause actual results to differ from expectations include those described below:

General economic or business conditions, either nationally or in California, may be less favorable than expected, resulting in, among other things, a deterioration in credit quality or a reduced demand for credit;

Because our business is concentrated in California, changes in the economic conditions of the California market could adversely affect our operations;

Changes in the interest rate environment could adversely affect our banking and real estate investment activities;

Regulatory changes could have adverse effects on the financial services industry;

Competitive pressures among depository and other financial institutions may increase significantly;

Our competitors may have greater financial resources that enable them to compete more successfully than we can;

Federal monetary policy changes could have adverse effects on the financial services industry; or

We could experience greater than anticipated losses on our loans because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loans.

Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Actual results may differ from expectations due to many factors beyond our ability to control or predict, including those described above, and in documents incorporated by reference in this prospectus. For these statements, Downey Financial Corp. and Downey Financial Capital Trusts II and III claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

You should rely only on the information contained and incorporated by reference in this prospectus and the accompanying prospectus supplement. We have not authorized anyone to provide you with information different from that contained or incorporated by reference in this prospectus and the accompanying prospectus supplement. Downey and the trusts are offering to sell securities and seeking offers to buy securities only in jurisdictions where offers and sales are permitted. The information contained and incorporated by reference in this prospectus and the accompanying prospectus supplement is accurate only as of the date of this prospectus or the prospectus supplement or the date of the document incorporated by reference, as the case may be, regardless of the time of delivery of the prospectus or prospectus supplement or any sale of the securities.

WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports and proxy statements and other information with the SEC. You may read and copy any document which Downey Financial Corp. files at the SEC's public reference rooms in Washington, D.C., Chicago, Illinois and New York, New York. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. Our filings with the SEC are also

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available to the public over the Internet at a World Wide Web site maintained by the SEC at <http://www.sec.gov>. In addition, you may inspect our reports, proxy statements and other information at the offices of the New York Stock Exchange.

Downey Financial Corp. and the trusts have jointly filed with the SEC a Registration Statement on Form S-3 under the Securities Act with respect to the securities offered by this prospectus. This prospectus, which constitutes a part of the Registration Statement, does not contain all of the information shown in the Registration Statement. For further information with respect to Downey Financial Corp., the trusts and the securities offered by this prospectus, reference is made to the Registration Statement and the exhibits thereto which you may inspect at the public reference facilities of the SEC, at the address shown above, or through the SEC's Web site.

DOCUMENTS INCORPORATED BY REFERENCE

The SEC allows us to incorporate by reference information into this prospectus which means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be a part of this prospectus, and information that we file later with the SEC will automatically update and supersede this information. We incorporate by reference the documents listed below and any future filings made by us with the SEC which we may make under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 until we sell all of the securities offered hereby:

Annual Report on Form 10-K, as amended, for the year ended December 31, 1999; and

Quarterly Reports on Form 10-Q for the quarters ended March 31, 2000, June 30, 2000 and September 30, 2000.

You may request a copy of these incorporated filings, without charge, excluding all exhibits unless specifically incorporated by reference as an exhibit to this prospectus. You may request copies by writing or telephoning Downey Financial Corp., 3501 Jamboree Road, Newport Beach, California 92660, Attention: Corporate Secretary, telephone (949) 854-0300.

This prospectus does not contain or incorporate by reference any separate financial statements of the trusts. We do not consider that financial statements of the trusts are material to holders of the capital securities because each trust is a newly formed special purpose entity, has no operating history or independent operations and is not engaged in and does not propose to engage in any activity other than holding the junior subordinated debentures of Downey Financial Corp. and issuing the capital securities and the common securities. For more information, see the information under the captions Prospectus Summary Downey Financial Capital Trusts II and III, Description of the Capital Securities, Description of Junior Subordinated Debentures and Description of Guarantee. In addition, we do not expect that the trusts will be filing reports under the Securities Exchange Act of 1934 with the SEC.

USE OF PROCEEDS

Except as otherwise stated in any prospectus supplement, Downey will use the net proceeds from the sale of common stock, preferred stock and debt securities for general corporate purposes, which may include advances or investments in our subsidiaries, working capital, capital expenditures and repayment of existing indebtedness.

All of the proceeds from the sale of capital securities will be invested by the trusts in the junior subordinated debentures of Downey.

Table of Contents**RATIO OF EARNINGS TO FIXED CHARGES**

The following table sets forth our ratio of earnings to fixed charges on a consolidated basis for the periods specified.

	Nine Months Ended September 30,		Year Ended December 31,				
	2000	1999	1999	1998	1997	1996(1)	1995
Ratio of earnings to fixed charges:							
Excluding interest on deposits	2.11x	2.78x	2.47x	6.22x	2.96x	2.39x	2.15x