GOLD BANC CORP INC
Form 10-Q
May 15, 2002

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

ý **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended March 31, 2002

o **TRANSITION REPORT UNDER SECTION 13 OR 15(D) OF THE EXCHANGE ACT**
For the transition period from to

Commission File Number: 0-28936

GOLD BANC CORPORATION, INC.

(Exact name of registrant as specified in its charter)

Kansas	**48-1008593**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
11301 Nall Avenue, Leawood, Kansas	**66211**
(Address of principal executive office)	(Zip code)

(913) 451-8050
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for past 90 days. Yes o No o

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practical date.

Class	Outstanding at April 30, 2002
Common Stock, $1.00 par value	33,986,992

GOLD BANC CORPORATION, INC.
INDEX TO 10-Q FOR THE QUARTERLY
PERIOD ENDED MARCH 31, 2001

2

PART I
FINANCIAL INFORMATION
GOLD BANC CORPORATION, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
(In thousands)
(unaudited)

	Mar. 31, 2002	Dec. 31, 2001
Assets		
Cash and due from banks	$ 66,784	$ 73,675
Federal funds sold and interest-bearing deposits	56,393	98
Total cash and cash equivalents	123,177	73,773

	Mar. 31, 2002	Dec. 31, 2001
Investment securities:		
Available-for-sale	546,554	567,746
Held-to-maturity	23,466	14,364
Trading	2,763	6,734
Total investment securities	572,783	588,844
Mortgage loans held for sale, net	39,500	11,335
Loans, net	2,277,470	2,124,973
Premises and equipment, net	67,730	57,738
Goodwill, net	34,610	34,610
Intangible assets	3,983	4,110
Cash surrender value of bank owned life insurance	54,141	53,038
Accrued interest and other assets	61,773	68,051
Total assets	$ 3,235,167	$ 3,016,472
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits	$ 2,380,331	$ 2,163,866
Securities sold under agreements to repurchase	104,498	103,672
Federal funds purchased and other short-term borrowings	1,083	30,908
Guaranteed preferred beneficial interests in Company's debentures	111,749	111,749
Long-term borrowings	447,626	416,413
Accrued interest and other liabilities	26,622	24,219
Total liabilities	3,071,909	2,850,827
Stockholders' equity:		
Preferred stock, no par value; 50,000,000 shares authorized, no shares issued		
Common stock, $1.00 par value, 50,000,000 shares authorized 38,404,002 issued at March 31, 2002 and 38,352,074 issued at December 31, 2001	38,404	38,352
Additional paid-in capital	76,011	75,955
Retained earnings	90,957	85,721
Accumulated other comprehensive income (loss), net	(204)	(8)
Unearned compensation	(8,790)	(3,440)
	196,378	196,580
Less treasury stock 4,721,510 shares at March 31, 2002 and 4,417,010 shares at December 31, 2001	(33,120)	(30,935)
Total stockholders' equity	163,258	165,645
Total liabilities and stockholders' equity	$ 3,235,167	$ 3,016,472

See accompanying notes to consolidated financial statements.

GOLD BANC CORPORATION, INC. AND SUBSIDIARIES
Consolidated Statements of Earnings
For The Three Months Ended
(In thousands, except per share data)
(unaudited)

	Mar. 31, 2002	Mar. 31, 2001
Interest Income:		
Loans, including fees	$ 39,035	$ 44,144
Investment securities	8,337	7,131
Other	595	1,711
	47,967	52,986
Interest Expense:		
Deposits	15,397	24,324
Borrowings and other	8,441	6,403
	23,838	30,727
Net interest income	24,129	22,259
Provision for loan losses	5,035	2,545
Net interest income after provision for loan losses	19,094	19,714
Other income:		
Service fees	3,970	2,595
Investment trading fees and commissions	1,396	1,467
Net gains on sale of mortgage loans	696	870
Net securities gains	534	979
Information technology services	4,876	1,393
Other	2,354	2,708
	13,826	10,012
Other expense:		
Salaries and employee benefits	11,948	10,605
Net occupancy expense	1,478	1,464
Depreciation expense	1,509	1,548
Goodwill amortization expense		530
Information technology services	3,171	795
Other	6,694	5,480
	24,800	20,422
Earnings before income tax	8,120	9,304
Income tax expense	2,113	3,334
Net earnings	$ 6,007	$ 5,970

	Mar. 31, 2002	Mar. 31, 2001
Net earnings per share basic and diluted	$ .18	$ .16

See accompanying notes to consolidated financial statements

4

GOLD BANC CORPORATION, INC. AND SUBSIDIARIES
Consolidated Statements of Stockholders' Equity and Comprehensive Income
Period ended March 31, 2002 and December 31, 2001
(Dollars in thousands)

	Preferred stock	Common Stock	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income (loss)	Unearned compensation	Treasury stock	Total
Balance at December 31, 2000		38,286	75,523	64,198	836	(3,802)	(5,795)	162,246
Net income for 2001				5,970				5,970
Change in unrealized gain on available-for-sale securities					519			519
Total comprehensive income for 2001				5,970	519			6,489
Exercise of 36,887 stock options		37	173					210
Purchase of 874,000 shares of treasury stock							(5,397)	(5,397)
Decrease in unearned compensation								
Dividends paid ($0.02 per common share)				(735)				(735)
Balance at March 31, 2001		38,323	75,696	69,433	1,355	(3,802)	(11,192)	169,813
Balance at December 31, 2001		38,352	75,955	85,721	(8)	(3,440)	(30,935)	165,645
Net earnings for 2002				6,007				6,007
Change in unrealized gain on available-for-sale securities					(196)			(196)
Total comprehensive income for 2001				6,007	(196)			5,811
Exercise of 51,927 stock options		52	56					108
Purchase of 304,500 shares of treasury stock							(2,185)	(2,185)
Decrease in unearned compensation						(5,350)		(5,350)
Dividends paid ($0.08 per common share)				(771)				(771)
Balance at December 31, 2001	$	38,404	76,011	90,957	(204)	(8,790)	(33,120)	163,258

See accompanying notes to consolidated financial statements.

5

GOLD BANC CORPORATION, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Three Months Ended

(In thousands)
(unaudited)

	March 31, 2002	March 31, 2001
Cash flows from operating activities:		
Net Earnings	$ 6,007	$ 5,970
Adjustments to reconcile net earnings to net cash provided by (used in)		
Operating activities, net of purchase acquisitions:		
Provision for loan losses		2,545
(Gains) on sales of securities	(534)	(979)
Amortization of investment securities' premiums, net of accretion	(19)	(136)
Depreciation	1,509	1,548
Amortization of intangible assets	127	
Amortization of goodwill		530
(Gain) on sale of mortgage loans, net	(696)	(870)
Bank owned life insurance	(1,103)	
Net (increase) decrease in trading securities	3,971	1,548
Proceeds from sale of loans held for sale	28,058	58,522
Origination of loans held for sale, net of repayments	(55,623)	(17,862)
Other changes:		
Accrued interest receivable and other assets	6,278	7,034
Accrued interest payable and other liabilities	2,704	(548)
Net cash provided by (used in) operating activities	(4,286)	57,312
Cash flows from investing activities:		
Net increase in loans	(157,532)	(35,642)
Principal collections and proceeds from maturities of held-to-maturity securities	200	1,179
Principal collections and proceeds from sales and maturities of available-for-sale securities	232,646	215,424
Purchases of available-for-sale securities	(211,527)	(174,423)
Purchases of held-to-maturity securities	(9,306)	
Net additions to premises and equipment	(11,501)	(605)
Proceeds from sale of other assets		
Cash paid, net of cash received, in purchase acquisition		(2,490)
Net cash provided by (used) in investing activities	(157,020)	3,443
Cash flows from financing activities:		
Increase (decrease) in deposits	216,465	(32,345)
Net increase (decrease) in short-term borrowings	(28,999)	36,146
Proceeds From FHLB & long-term borrowings	25,863	
Payment on FHLB & long-term borrowings		(27,298)
Proceeds from issuance of common stock	241	210
Purchase of treasury stock	(2,185)	(5,397)
Dividends paid	(675)	(735)
Net cash provided by (used) in financing activities	210,710	(29,419)
Increase (decrease) in cash and cash equivalents	49,404	31,336
Cash and cash equivalents, beginning of period	73,773	118,891

	March 31, 2002	March 31, 2001
Cash and cash equivalents, end of period	$ 123,177	$ 150,227
Supplemental schedule of non-cash activities:		
Non-cash investing activities related to the securitization of loans held for sale:		
Increase in investment securities		$ 27,733
Decrease in mortgage loans held for sale		27,733
Non-cash activities related to purchase acquisitions:		
Increase in land, buildings, and equipment		$ 38
Increase in other assets		1,600
Increase in other liabilities		17
Increase in trading securities		835
Supplemental Disclosure of Cash Flow Information:		
Cash paid for Interest	24,071	31,973
Cash paid for Income Taxes	1,717	2,734

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of presentation.

The accompanying consolidated financial statements have been prepared in accordance with the instructions for Form 10-Q. The consolidated financial statements should be read in conjunction with the audited financial statements included in the Company's 2001 Annual Report on Form 10-K.

The consolidated financial statements include the accounts of Gold Banc Corporation, Inc. and its subsidiary banks and companies, collectively referred to as the Company. All significant intercompany balances and transactions have been eliminated.

The consolidated financial statements as of March 31, 2002 and for the three months ended March 31, 2002 and 2001 are unaudited but include all adjustments (consisting only of normal recurring adjustments) which the Company considers necessary for a fair presentation of financial position and results of its operations and its cash flows for those periods. The Consolidated Statement of Earnings for the three months ended March 31, 2002 is not necessarily indicative of the results to be expected for the entire year.

2. Earnings per common share.

Earnings per share are computed in accordance with SFAS No. 128, *Earnings per Share*. Basic earnings per share is based upon the weighted average number of common shares outstanding during the periods presented. Diluted earnings per share includes the effects of all potentially dilutive common shares outstanding during each period. Employee stock options are the Company's only potential common share equivalent.

The shares used in the calculation of basic and diluted income per share for the three months ended March 31, 2002 and 2001 are shown below (in thousands):

	2002	2001
Weighted average common shares outstanding	33,733	37,000
Stock options	65	38
Weighted average common shares and Common share equivalents outstanding	33,798	37,038

3.

Intangible Assets and Goodwill

The following table presents information about the Company's intangible assets which are being amortized in accordance with Statement of Financial Accounting Standards (SFAS) No. 142.

	March 31, 2002 Gross Carrying Amount	March 31, 2002 Accumulated Amortization	March 31, 2001 Gross Carrying Amount	March 31, 2001 Accumulated Amortization
	(In thousands)			
Amortized intangible assets:				
Core deposit premium	$ 4,900	$ 917	$	$
Total	$ 4,900	$ 917	$	$
Aggregate amortization expense for the Three-months ended	7	$ 127		$

Estimated amortization expense for the Years ended:

2002	$277,085
2003	$277,085
2004	$277,085
2005	$277,085
2006	$277,085

As required by SFAS 142, the Company discontinued recording goodwill amortization effective January 1, 2002. The following tables compare results of operations as if no goodwill amortization had been recorded in 2001.

	For the Three Months Ended March 31 2002	For the Three Months Ended March 31 2001
	(In thousands except per share data)	
Reported net income	$ 6,007	5,970
Add back goodwill amortization		530
Adjusted net income	$ 6,007	$ 6,500
Basic earnings per share:		
Reported net income	$ 0.18	$ 0.16
Add back goodwill amortization		0.01
Adjusted net income	$ 0.18	$ 0.17
Diluted earnings per share		
Reported net income	$ 0.18	$ 0.16
Add back goodwill amortization		0.01
Adjusted net income	$ 0.18	$ 0.17

4.

Comprehensive Income.

Comprehensive income was $5.8 million and $6.5 million for the three months ended March 31, 2002 and 2001, respectively. The difference between comprehensive income and net earnings presented in the Consolidated Statement of Earnings is attributed solely to unrealized gains and losses on available-for-sale securities. During the three months ended March 31, 2002, and 2001, the Company recorded reclassification adjusments of $342,000 and 626,000 associated with gains included in net income for the period.

5.

Mergers, Acquisitions, Dispositions and Consolidations

Ott Financial Corporation. On March 30, 2001, Gold Capital Management, our wholly owned subsidiary, acquired Ott Financial Corporation of Wichita, Kansas for approximately $2.7 million. Ott was the holding company for Davidson Securities, Inc. and J.O. Davidson and Associates, Inc., which specialized in public finance advisory and underwriting services. At the time of the acquisition, the companies were all merged into Gold Capital Management. The acquisition was accounted for using the purchase method of accounting. The excess of cost over fair value of the underlying net assets acquired was $1.5 million. Ott had total assets of approximately $1.3 million at the time of the acquisition.

Information Products, Inc. On April 26, 2001, CompuNet Engineering, a wholly owned subsidiary of our Company, acquired the assets of Information Products for approximately $1 million. Information Products provides technology services, including LAN, WAN, product support, telecommunication line

monitoring, hardware maintenance and systems design and installation across all industry sectors. The asset acquielopment Corp., Ser
2009 6.25 07/15/40 844,223 340

Brooklyn Arena Local Development Corp., Ser 2009
6.375 07/15/43 348,653 2,380
City of New York, 2009 Subser A-1 (a)
5.25 08/15/27 2,559,082 2,380
City of New York, 2009 Subser A-1 (a)
5.25 08/15/28 2,559,082 10,000
Metropolitan Transportation Authority, Transportation Refg Ser 2002 A (NATL-RE & FGIC Insd)
5.00 11/15/25 10,312,100 3,500
New York City Municipal Water Finance Authority, Ser 2002 A
5.375 06/15/19 3,799,285 18,000
New York City Municipal Water Finance Authority, Ser 2002 B (a)
5.00 06/15/26 18,422,820 3,000
New York City Municipal Water Finance Authority, Ser 2003 A
5.00 06/15/35 3,050,130 2,040
New York City Transitional Finance Authority, 2010 Subser A-1 (a)
5.00 05/01/28 2,179,325 1,635
New York City Transitional Finance Authority, 2010 Subser A-1 (a)
5.00 05/01/29 1,746,665 1,635
New York City Transitional Finance Authority, 2010 Subser A-1 (a)
5.00 05/01/30 1,746,665 1,935
New York City Trust for Cultural Resources, Museum of Modern Art Refg Ser 2008 1A (a)
5.00 04/01/26 2,096,000 2,815
New York City Trust for Cultural Resources, Museum of Modern Art Refg Ser 2008 1A (a)
5.00 04/01/27 3,049,220 1,100
New York State Dormitory Authority, New York University (AMBAC Insd)
5.50 05/15/29 1,197,548 2,000
Seneca Nation Indians, Ser 2007 A (f)
5.00 12/01/23 1,654,640 5,000
Tobacco Settlement Financing Corp., Ser 2003 B-1C
5.50 06/01/17 5,226,400 5,000
Triborough Bridge & Tunnel Authority, Refg 2002 E (NATL-RE
Insd) (a)

5.25 11/15/22 5,358,649

66,150,487

North Carolina (1.6%)

4,500

City of Charlotte, Water/Sewer Ser 2001

5.125 06/01/26 4,674,285

North Dakota (0.8%)

2,750

County of Ward, Trinity Ser 2006

5.125 07/01/29 2,441,422

Morgan Stanley Quality Municipal Income Trust*
Portfolio of Investments § January 31, 2010 (unaudited) *continued*

PRINCIPAL AMOUNT IN THOUSANDS		COUPON RATE	MATURITY DATE	VALUE
	Ohio (5.5%)			
$ 5,100	American Municipal Power-Ohio Inc., Prairie State Energy Campus Ser 2008 A (AGC Insd) (a)	5.25%	02/15/33	$ 5,307,379
5,370	County of Cuyahoga, Cleveland Clinic Ser 2003 A	6.00	01/01/32	5,636,513
3,000	County of Lorain, Catholic Healthcare Partners Ser 2001 A	5.625	10/01/17	3,108,960
2,000	Ohio State University, General Receipts Ser 2002 A	5.125	12/01/31	2,055,980
410	Ohio State Water Development Authority, Ser 2009 A	5.875	06/01/33	446,490
				16,555,322
	Oklahoma (0.4%)			
1,500	Oklahoma Development Finance Authority, Great Plains Regional Medical Center Ser 2007	5.125	12/01/36	1,257,810
	Oregon (0.3%)			
685	Oregon State Department of Administrative Services, Ser 2009 A	5.25	04/01/24	774,303
	Pennsylvania (1.0%)			
4,000	Allegheny County Hospital Development Authority, West Penn Allegheny Health Ser 2007 A	5.375	11/15/40	2,962,200
	Puerto Rico (1.4%)			
1,375	Puerto Rico Sales Tax Financing Corp., Ser 2009 A	5.00	08/01/39	1,444,272
1,225	Puerto Rico Sales Tax Financing Corp., Ser 2010 A (e)	5.375	08/01/39	1,209,810
1,400	Puerto Rico Sales Tax Financing Corp., Ser 2010 A (e)	5.50	08/01/42	1,389,514
				4,043,596
	South Carolina (5.4%)			
3,000	Charleston Educational Excellence Finance Corp., Charleston County School District Ser 2005	5.25	12/01/29	3,097,110
345	County of Richland, Environmental Improvement, Paper Co. Ser 2007 A	4.60	09/01/12	349,437
70	Lexington County Health Services District, Inc., Ser 2007 A	5.00	11/01/16	75,578
5,000	South Carolina State Public Service Authority, Refg Ser 2002 D (AGM Insd)	5.00	01/01/20	5,334,450
7,000	South Carolina State Public Service Authority, Santee Cooper Ser 2003 A (AMBAC Insd) (a)	5.00	01/01/22	7,380,805
				16,237,380
	Tennessee (0.6%)			
1,620	Tennessee Energy Acquisition Corp., Ser 2006 A	5.25	09/01/19	1,649,614

	Texas (20.4%)			
2,000	Alliance Airport Authority, Federal Express Corp. Refg Ser 2006 (AMT)	4.85	04/01/21	1,975,100
1,045	Bexar County Health Facilities Development Corp. (e)	6.20	07/01/45	1,048,908
2,500	City of Arlington, Special Tax Ser 2009	5.00	08/15/28	2,541,775
10,000	City of Austin, Water & Wastewater Refg Ser 2001 A & B (AGM Insd) (a)	5.125	05/15/27	10,341,142
6,000	City of Houston, Airport Sub Lien Ser 2000 A (AMT) (AGM Insd)	5.875	07/01/17	6,091,500
5,120	City of Houston, Combined Utility First Lien Refg 2004 Ser A (NATL-RE & FGIC Insd)	5.25	05/15/23	5,405,696
2,000	City of Houston, Ser 2009 A	5.00	03/01/27	2,141,640
5,000	City of Houston, Ser A 2001 (AMT) (AGM Insd)	5.625	07/01/30	5,008,750
8,960	City of San Antonio, (NATL-RE & FGIC Insd)	5.00	05/15/26	9,183,194
2,500	County of Bexar, Ser 2009 A	5.00	06/15/35	2,589,800
2,380	County of Harris, Ser 2007 C (AGM Insd)	5.25	08/15/31	2,731,954
600	Harris County Industrial Development Corp., Deer Park Refinancing Project	5.00	02/01/23	599,940

Morgan Stanley Quality Municipal Income Trust*
Portfolio of Investments § January 31, 2010 (unaudited) *continued*

PRINCIPAL AMOUNT IN THOUSANDS		COUPON RATE	MATURITY DATE	VALUE
$ 8,600	North Texas Tollway Authority, Refg Ser 2008 D (AGC Insd) (b)	0.00%	01/01/28	$ 3,097,376
1,650	North Texas Tollway Authority, Refg Ser 2008 D (AGC Insd) (b)	0.00	01/01/31	486,833
2,000	Tarrant County Cultural Education Facilities Finance Corp., Air Force Village II Inc Ser 2007	5.125	05/15/37	1,666,040
915	Texas Private Activity Bond Surface Transportation Corp., Senior Lien	6.875	12/31/39	956,605
5,100	University of Houston/TX, Ser 2008 (AGM Insd) (a)	5.00	02/15/33	5,235,762
				61,102,015
	Vermont (0.7%)			
2,500	Vermont Economic Development Authority, Wake Robin Corp Ser 2006 A	5.375	05/01/36	2,066,350
	Virginia (1.5%)			
2,000	Fairfax County Economic Development Authority, Goodwin House, Inc. Ser 2007	5.125	10/01/42	1,811,120
1,450	Henrico County Economic Development Authority, Residential Care Facility, Westminster Cantebury-Management Corp. Ser 2006	5.00	10/01/27	1,268,866
1,750	Henrico County Economic Development Authority, Residential Care Facility, Westminster Cantebury-Management Corp. Ser 2006	5.00	10/01/35	1,452,552
				4,532,538
	Washington (8.6%)			
5,000	Energy Northwest, Ser 2002 A (NATL-RE Insd)	5.75	07/01/18	5,478,450
5,000	Grant County Public Utility District No. 2, Electric Refg Ser 2001 H (AGM Insd)	5.375	01/01/18	5,340,100
2,510	Port of Seattle, Passenger Facility Ser 1998 A (NATL-RE Insd)	5.00	12/01/23	2,516,200
2,500	Spokane County School District No. 81, Ser 2005 (NATL-RE Insd)	5.125	06/01/23	2,667,550
3,725	State of Washington, Various Purpose Ser 2010 A (a)	5.00	08/01/29	3,979,141
3,915	State of Washington, Various Purpose Ser 2010 A (a)	5.00	08/01/30	4,182,104
1,500	Washington Health Care Facilities Authority, Providence Health Ser 2006 C (AGM Insd)	5.25	10/01/33	1,538,790
				25,702,335
	Total Tax-Exempt Municipal Bonds *(Cost $500,095,767)*			501,159,042

NUMBER OF

SHARES (000)			
	Short-Term Investment (g) (3.1%)		
	Investment Company		
9,199	Morgan Stanley Institutional Liquidity Funds Tax Exempt Portfolio Institutional Class *(Cost $9,198,512)*		9,198,512
	Total Investments *(Cost $509,294,279) (h)(i)*	170.4%	510,357,554
	Liabilities in Excess of Other Assets	(0.5)	(1,521,750)
	Floating Rate Note and Dealer Trusts Obligations Related to Securities Held		
	Notes with interest rates ranging from 0.16% to 0.25% at January 31, 2010 and contractual maturity dates of collateral ranging from 01/01/22 to 01/01/37 (j)	(23.9)	(71,659,000)
	Preferred Shares of Beneficial Interest	(46.0)	(137,650,000)
	Net Assets Applicable to Common Shareholders	100.0%	$ 299,526,804

Note: The categories of investments are shown as a percentage of net assets applicable to common shareholders.

AMT *Alternative Minimum Tax.*

BANs *Bond Anticipation Notes.*

Morgan Stanley Quality Municipal Income Trust*
Portfolio of Investments § January 31, 2010 (unaudited) *continued*

COPs	*Certificates of Participation.*
CR	*Custodial Receipts.*
(a)	*Underlying security related to inverse floater entered into by the Trust.*
(b)	*Capital appreciation bond.*
(c)	*Prefunded to call date shown.*
(d)	*Security is subject to a shortfall agreement which may require the Trust to pay amounts to a counterparty in the event of a significant decline in the market value of the security underlying the inverse floater. In case of a shortfall, the maximum potential amount of payments the Trust could ultimately be required to make under the agreement is $7,335,000. However, such shortfall payment would be reduced by the proceeds from the sale of the security underlying the inverse floater.*
(e)	*Security purchased on a when-issued basis.*
(f)	*Resale is restricted to qualified institutional investors.*
(g)	*The Trust invests in Morgan Stanley Institutional Liquidity Funds Tax-Exempt Portfolio Institutional Class, an open-end management investment company managed by the Investment Adviser. Investment advisory fees paid by the Trust are reduced by an amount equal to the advisory and administrative service fees paid by Morgan Stanley Institutional Liquidity Funds Tax-Exempt Portfolio Institutional Class with respect to assets invested by the Trust in Morgan Stanley Institutional Liquidity Funds Tax-Exempt Portfolio Institutional Class.*
(h)	*Securities have been designated as collateral in connection with securities purchased on a when-issued basis and inverse floating rate municipal obligations.*
(i)	*The aggregate cost for federal income tax purposes approximates the aggregate cost for book purposes.*
(j)	*Floating rate note obligations related to securities held The Trust enters into transactions in which it transfers to Dealer Trusts (Dealer Trusts), fixed rate bonds in exchange for cash and residual interests in the Dealer Trusts assets and cash flows, which are in the form of inverse floating rate investments. The Dealer Trusts fund the purchases of the fixed rate bonds by issuing floating rate notes to third parties and allowing the Trust to retain residual interest in the bonds. The Trust enters into shortfall agreements with the Dealer Trusts which commit the Trust to pay the Dealer Trusts, in certain circumstances, the difference between the liquidation value of the fixed rate bonds held by the Dealer Trusts and the liquidation value of the floating rate notes held by third parties, as well as any shortfalls in interest cash flows. The residual interests held by the Trust (inverse floating rate investments) include the right of the Trust (1) to cause the holders of the floating rate notes to tender their notes at par at the next interest rate reset date, and (2) to transfer the municipal bond from the Dealer Trusts to the Trust, thereby collapsing the Dealer Trusts. The Trust accounts for the transfer of bonds to the Dealer Trusts as secured borrowings, with the securities transferred remaining in the Trust s investment assets, and the related floating rate notes reflected as Trust liabilities. The notes issued by the Dealer Trusts have interest rates*

that reset weekly and the floating rate note holders have the option to tender their notes to the Dealer Trusts for redemption at par at each reset date. At January 31, 2010, the Trust s investments with a value of $115,864,902 are held by the Dealer Trusts and serve as collateral for the $71,659,000 in floating rate note and dealer trusts obligations outstanding at that date.

Bond Insurance:

AGC	*Assured Guaranty Corporation.*
AGM	*Assured Guaranty Municipal Corporation.*
AMBAC	*AMBAC Assurance Corporation.*
BHAC	*Berkshire Hathaway Assurance Corporation.*
FGIC	*Financial Guaranty Insurance Company.*
NATL-RE	*National Public Finance Guarantee Corporation.*
XLCA	*XL Capital Assurance Inc.*

Morgan Stanley Quality Municipal Income Trust*
Notes to the Portfolio of Investments § January 31, 2010 (unaudited)
Fair Valuation Measurements

Fair value is defined as the price that the Trust would receive to sell an investment or pay to transfer a liability in a timely transaction with an independent buyer in the principal market, or in the absence of a principal market the most advantageous market for the investment or liability. GAAP utilizes a three-tier hierarchy to distinguish between (1) inputs that reflect the assumptions market participants would use in pricing an asset or liability developed based on market data obtained from sources independent of the reporting entity (observable inputs) and (2) inputs that reflect the reporting entity s own assumptions about the assumptions market participants would use in pricing an asset or liability developed based on the best information available in the circumstances (unobservable inputs) and to establish classification of fair value measurements for disclosure purposes. Various inputs are used in determining the value of the Trust s investments. The inputs are summarized in the three broad levels listed below.

Level 1 unadjusted quoted prices in active markets for identical investments

Level 2 other significant observable inputs (including quoted prices for similar investments, interest rates, prepayment speeds, credit risk, etc.)

Level 3 significant unobservable inputs (including the Trust s own assumptions in determining the fair value of investments)

The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities and the determination of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to each security.

The following is the summary of the inputs used as of January 31, 2010 in valuing the Trust s investments carried at fair value:

		FAIR VALUE MEASUREMENTS AT JANUARY 31, 2010 USING		
INVESTMENT TYPE	**TOTAL**	**UNADJUSTED QUOTED PRICES IN ACTIVE MARKET FOR IDENTICAL INVESTMENTS (LEVEL 1)**	**OTHER SIGNIFICANT OBSERVABLE INPUTS (LEVEL 2)**	**SIGNIFICANT UNOBSERVABLE INPUTS (LEVEL 3)**
Tax-Exempt Municipal Bonds	$ 501,159,042		$ 501,159,042	
Short-Term Investment Investment Company	9,198,512	$ 9,198,512		
Total	$ 510,357,554	$ 9,198,512	$ 501,159,042	

Valuation of Investments (1) portfolio securities are valued by an outside independent pricing service approved by the Trustees. The pricing service uses both a computerized grid matrix of tax-exempt securities and evaluations by its staff, in each case based on information concerning market transactions and quotations from dealers which reflect the mean between the last reported bid and ask price. The portfolio securities are thus valued by reference to a combination of transactions and quotations for the same or other securities believed to be comparable in quality, coupon, maturity, type of issue, call provisions, trading characteristics and other features deemed to be relevant. The Trustees believe that timely and reliable market quotations are generally not readily available for purposes of valuing tax-exempt securities and that the valuations supplied by the pricing service are more likely to represent the fair value of such securities; (2) futures are valued at the latest sale price on the commodities exchange on which they trade unless it is determined that such price does not reflect their market value, in which case they will be valued at their fair value as determined in good faith under procedures established by and under the supervision of the Trustees; (3) interest rate swaps are marked-to-market daily based upon quotations from market makers; (4) investments in open-end mutual funds, including the Morgan Stanley Institutional Liquidity Funds, are valued at the net asset value as of the close of each business day; and (5) short-term debt securities having a maturity date of more than sixty days at time of purchase are valued on a mark-to-market basis until sixty days prior to maturity and thereafter at amortized cost based on their value on the 61st day. Short-term debt securities having a maturity date of sixty days or less at the time of purchase are valued at amortized cost, which approximates market value.

* Morgan Stanley announced on October 19, 2009 that it has entered into a definitive agreement to sell substantially all of its retail asset management business to Invesco Ltd. (Invesco), a leading global investment management company. The Trustees of the Trust approved an Agreement and Plan of Reorganization (the Plan). Pursuant to the Plan, substantially all of the assets of the Trust would be combined with those of a newly organized mutual fund advised by an affiliate of Invesco Ltd. (the New Trust). Pursuant to the Plan, shareholders of the Trust would become shareholders of the New Trust, receiving shares of such New

Trust equal to the value of their holdings in the Trust. The Plan is subject to the approval of the Trust s shareholders at a special meeting of shareholders anticipated to be held during the second quarter of 2010.

Item 2. Controls and Procedures.

(a) The Trust s principal executive officer and principal financial officer have concluded that the Trust s disclosure controls and procedures are sufficient to ensure that information required to be disclosed by the Trust in this Form N-Q was recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms, based upon such officers evaluation of these controls and procedures as of a date within 90 days of the filing date of the report.

(b) There were no changes in the Trust s internal control over financial reporting that occurred during the registrant s fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Trust s internal control over financial reporting.

Item 3. Exhibits.

(a) A separate certification for each principal executive officer and principal financial officer of the registrant are attached hereto.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Morgan Stanley Quality Municipal Income Trust
/s/ Randy Takian
Randy Takian
Principal Executive Officer
March 23, 2010

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

/s/ Randy Takian
Randy Takian
Principal Executive Officer
March 23, 2010
/s/ Francis Smith
Francis Smith
Principal Financial Officer
March 23, 2010