

PMC COMMERCIAL TRUST /TX

Form 10-Q

May 15, 2006

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10 - Q**

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

For the quarterly period ended **March 31, 2006**

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

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

Commission File Number 1-13610

**PMC COMMERCIAL TRUST**

(Exact name of registrant as specified in its charter)

TEXAS

75-6446078

(State or other jurisdiction  
of incorporation or organization)

(I.R.S. Employer Identification No.)

17950 Preston Road, Suite 600, Dallas, TX  
75252

(972) 349-3200

(Address of principal executive offices)

(Registrant's telephone number)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO   
Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the Registrant is a well-known seasoned issuer (as defined in Rule 405 of the Securities Act). YES  NO

Indicate by check mark whether the Registrant is a shell company (as defined in Exchange Act Rule 12b-2). YES  NO

As of May 8, 2006, the Registrant had outstanding 10,741,921 Common Shares of Beneficial Interest, par value \$.01 per share.

**PMC COMMERCIAL TRUST AND SUBSIDIARIES  
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**PART I**

**Financial Information**

**ITEM 1.**

**Financial Statements**

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**PMC COMMERCIAL TRUST AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
*(In thousands, except share data)*

	<b>March 31, 2006</b>	<b>December 31, 2005</b>
	<i>(Unaudited)</i>	
<b>ASSETS</b>		
Loans receivable, net	\$ 157,498	\$ 157,574
Retained interests in transferred assets	60,571	62,991
Real estate investments held for sale, net	6,708	15,470
Real estate investments, net	6,240	8,080
Restricted investments	4,457	3,532
Cash and cash equivalents	3,969	3,967
Rent and related receivables, net	1,192	1,489
Mortgage-backed security of affiliate	820	833
Deferred tax asset, net	385	349
Other assets	5,516	4,907
<b>Total assets</b>	<b>\$ 247,356</b>	<b>\$ 259,192</b>

**LIABILITIES AND BENEFICIARIES EQUITY**

<b>Liabilities:</b>		
Junior subordinated notes	\$ 27,070	\$ 27,070
Notes and debentures payable	23,161	26,900
Credit facilities	20,705	24,205
Borrower advances	4,814	4,418
Redeemable preferred stock of subsidiary	3,598	3,575
Dividends payable	3,284	3,293
Accounts payable and accrued expenses	2,229	2,920
Debt and accrued expenses — real estate investments held for sale	1,771	6,273
Deferred income	863	749
Due to affiliates, net	31	856
Other liabilities	1,048	1,016
<b>Total liabilities</b>	<b>88,574</b>	<b>101,275</b>

*Commitments and contingencies*

Cumulative preferred stock of subsidiary	900	900
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**Beneficiaries equity:**

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Common shares of beneficial interest; authorized 100,000,000 shares of \$0.01 par value; 11,028,271 shares issued at March 31, 2006 and December 31, 2005, 10,741,921 and 10,766,021 shares outstanding at March 31, 2006 and December 31, 2005, respectively	110	110
Additional paid-in capital	152,064	152,047
Net unrealized appreciation of retained interests in transferred assets	3,852	4,519
Cumulative net income	127,341	122,300
Cumulative dividends	(122,254)	(119,031)
	161,113	159,945
Less: Treasury stock; at cost, 286,350 shares and 262,250 shares at March 31, 2006 and December 31, 2005, respectively	(3,231)	(2,928)
<b>Total beneficiaries equity</b>	157,882	157,017
<b>Total liabilities and beneficiaries equity</b>	\$ 247,356	\$ 259,192

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

**PMC COMMERCIAL TRUST AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**  
*(In thousands, except per share data)*

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2006</b>	<b>2005</b>
	<i>(Unaudited)</i>	
<b>Revenues:</b>		
Interest income	\$ 3,682	\$ 2,487
Income from retained interests in transferred assets	2,253	2,527
Hotel property revenues	434	
Lease income	58	299
Other income	874	957
Total revenues	7,301	6,270
<b>Expenses:</b>		
Interest	1,460	1,032
Salaries and related benefits	1,060	1,055
General and administrative	607	597
Hotel property expenses	383	
Provision for loss on rent and related receivables	300	
Depreciation	62	81
Provision for loan losses, net	51	153
Realized losses on retained interests in transferred assets	48	21
Total expenses	3,971	2,939
<b>Income before income tax provision, minority interest and discontinued operations</b>	<b>3,330</b>	<b>3,331</b>
Income tax provision	(84)	(158)
Minority interest (preferred stock dividend of subsidiary)	(22)	(22)
<b>Income from continuing operations</b>	<b>3,224</b>	<b>3,151</b>
<b>Discontinued operations:</b>		
Net gains on sales of real estate	1,877	136
Impairment losses	(73)	
Net earnings	13	829
	1,817	965

<b>Net income</b>	\$ 5,041	\$ 4,116
 <i>Weighted average shares outstanding:</i>		
Basic	10,746	10,877
Diluted	10,746	10,891
 <i>Basic and diluted earnings per share:</i>		
Income from continuing operations	\$ 0.30	\$ 0.29
Discontinued operations	0.17	0.09
Net income	\$ 0.47	\$ 0.38

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



**PMC COMMERCIAL TRUST AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
*(In thousands)*

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2006</b>	<b>2005</b>
	<i>(Unaudited)</i>	
<b>Net income</b>	\$ 5,041	\$ 4,116
Change in unrealized appreciation (depreciation) of retained interests in transferred assets:		
Net unrealized depreciation arising during period	(489)	(1,384)
Net realized gains included in net income	(178)	(171)
	(667)	(1,555)
<b>Comprehensive income</b>	\$ 4,374	\$ 2,561

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

**PMC COMMERCIAL TRUST AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF BENEFICIARIES EQUITY**  
*(In thousands, except share and per share data)*

**Three Months Ended March 31, 2005**

*(Unaudited)*

	<b>Common</b>		<b>Net Unrealized Appreciation of Retained Interests</b>			<b>Cumulative</b>		<b>Total</b>
	<b>Shares of</b>		<b>Additional</b>	<b>in</b>	<b>Net</b>	<b>Cumulative</b>	<b>Treasury</b>	<b>Beneficiaries</b>
	<b>Beneficial</b>	<b>Par</b>	<b>Paid-in</b>	<b>Transferred</b>	<b>Income</b>	<b>Dividends</b>	<b>Stock</b>	<b>Equity</b>
	<b>Interest</b>	<b>Value</b>	<b>Capital</b>	<b>Assets</b>				
	<b>Outstanding</b>							
<b>Balances, December 31, 2004</b>	10,876,961	\$ 110	\$ 151,818	\$ 5,120	\$ 111,003	\$ (105,462)	\$ (1,285)	\$ 161,304
Net unrealized depreciation				(1,555)				(1,555)
Shares issued through exercise of stock options	3,000		39					39
Dividends (\$0.35 per share)						(3,807)		(3,807)
Net income					4,116			4,116
<b>Balances, March 31, 2005</b>	10,879,961	\$ 110	\$ 151,857	\$ 3,565	\$ 115,119	\$ (109,269)	\$ (1,285)	\$ 160,097

**Three Months Ended March 31, 2006**

*(Unaudited)*

	<b>Common</b>		<b>Net Unrealized Appreciation of Retained Interests</b>			<b>Cumulative</b>		<b>Total</b>
	<b>Shares of</b>		<b>Additional</b>	<b>in</b>	<b>Net</b>	<b>Cumulative</b>	<b>Treasury</b>	<b>Beneficiaries</b>
	<b>Beneficial</b>	<b>Par</b>	<b>Paid-in</b>	<b>Transferred</b>	<b>Income</b>	<b>Dividends</b>	<b>Stock</b>	<b>Equity</b>
	<b>Interest</b>	<b>Value</b>	<b>Capital</b>	<b>Assets</b>				
	<b>Outstanding</b>							
<b>Balances, December 31, 2005</b>	10,766,021	\$ 110	\$ 152,047	\$ 4,519	\$ 122,300	\$ (119,031)	\$ (2,928)	\$ 157,017
Net unrealized depreciation				(667)				(667)
Shares repurchased	(24,100)						(303)	(303)
Issuance of share options			17					17

Dividends (\$0.30 per share)						(3,223)		(3,223)
Net income					5,041			5,041

<b>Balances,</b>								
<b>March 31, 2006</b>	10,741,921	\$ 110	\$ 152,064	\$ 3,852	\$ 127,341	\$ (122,254)	\$ (3,231)	\$ 157,882

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

**PMC COMMERCIAL TRUST AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
*(In thousands)*

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2006</b>	<b>2005</b>
	<i>(Unaudited)</i>	
<b>Cash flows from operating activities:</b>		
Net income	\$ 5,041	\$ 4,116
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	71	437
Realized losses on retained interests in transferred assets	48	21
Net gains on sales of real estate	(1,877)	(136)
Deferred income taxes	(36)	(11)
Provision for loan losses	51	153
Provision for losses on rent and related receivables	300	
Impairment losses	73	
Premium income adjustment	8	29
Amortization and accretion, net	(41)	(106)
Share-based compensation	17	
Loans funded, held for sale	(860)	(1,555)
Proceeds from sale of guaranteed loans	418	1,940
Loan fees collected, net	80	152
Capitalized loan origination costs	(106)	(36)
Change in operating assets and liabilities:		
Due to/from affiliates, net	(825)	16
Other assets	(231)	(634)
Borrower advances	396	(149)
Accounts payable and accrued expenses	(710)	(519)
Other liabilities	(291)	(329)
<b>Net cash provided by operating activities</b>	<b>1,526</b>	<b>3,389</b>
<b>Cash flows from investing activities:</b>		
Loans funded	(3,766)	(6,696)
Principal collected on loans receivable	13,695	7,388
Principal collected on notes receivable		133
Principal collected on retained interests in transferred assets	1,712	1,700
Proceeds from assets acquired in liquidation held for sale, net	531	113
Proceeds from sales of hotel properties, net	2,529	2,012
Proceeds from mortgage-backed security of affiliate	13	37
Investment in retained interests in transferred assets		(818)
Investment in PMC Preferred Capital Trust-A		(820)
Investment in restricted investments, net	(925)	(344)
Purchase of furniture, fixtures and equipment	(29)	(160)
<b>Net cash provided by investing activities</b>	<b>13,760</b>	<b>2,545</b>

**Cash flows from financing activities:**

Proceeds from issuance of common shares		39
Purchase of treasury shares	(303)	
Repayment of revolving credit facility, net		(14,600)
Proceeds from issuance of SBA debentures		4,000
Proceeds from (repayment of) conduit warehouse facility, net	(3,500)	8,400
Proceeds from issuance of junior subordinated notes		27,070
Payment of principal on notes and mortgages payable and debentures	(8,249)	(27,302)
Payment of borrowing costs		(1,466)
Payment of dividends	(3,232)	(3,698)
<b>Net cash used in financing activities</b>	<b>(15,284)</b>	<b>(7,557)</b>
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>2</b>	<b>(1,623)</b>
<b>Cash and cash equivalents, beginning of year</b>	<b>3,967</b>	<b>9,065</b>
<b>Cash and cash equivalents, end of period</b>	<b>\$ 3,969</b>	<b>\$ 7,442</b>

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

**PMC COMMERCIAL TRUST AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
*(Unaudited)*

**Note 1. Interim Financial Statements:**

The accompanying consolidated balance sheet of PMC Commercial Trust ( PMC Commercial or together with its wholly-owned subsidiaries, we, us or our ) as of March 31, 2006 and the consolidated statements of income, comprehensive income, beneficiaries' equity and cash flows for the three months ended March 31, 2006 and 2005 have not been audited by independent accountants. In the opinion of management, the financial statements reflect all adjustments necessary to fairly present our financial position at March 31, 2006 and our results of operations for the three months ended March 31, 2006 and 2005. These adjustments are of a normal recurring nature.

Certain notes and other information have been omitted from the interim financial statements presented in this Quarterly Report on Form 10-Q. Therefore, these financial statements should be read in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2005.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect (1) the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and (2) the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates. Our most sensitive estimates involve the valuation of our retained interests in transferred assets, determination of reserves on our receivables and impairment analyses on our long-lived assets.

The results for the three months ended March 31, 2006 are not necessarily indicative of future financial results.

**Note 2. Business:**

PMC Commercial is a real estate investment trust ( REIT ) that either directly or through its subsidiaries, primarily originates loans to small businesses collateralized by first liens on the real estate of the related business. The majority of these loans are to borrowers in the hospitality industry. We also originate loans on commercial real estate to borrowers in the service, retail, multi-family and manufacturing industries and loans guaranteed by the Small Business Administration ( SBA ) collateralized by business assets and/or real estate. In addition, our investments include the ownership of commercial properties in the hospitality industry. Our common shares are traded on the American Stock Exchange under the symbol PCC.

**Note 3. Consolidation:**

We consolidate entities that we control by ownership of a majority voting interest as well as variable interest entities ( VIEs ) for which we are the primary beneficiary. To the extent we do not have a majority voting interest, we use the equity method to account for investments for which we have the ability to exercise significant influence over operating and financial policies. Consolidated net income includes our share of the net earnings of any entity accounted for using the equity method. The difference between consolidation and the equity method impacts certain financial ratios because of the presentation of the detailed line items reported in the financial statements. All material intercompany balances and transactions have been eliminated.

The consolidated financial statements include the accounts of PMC Commercial, First Western SBLC, Inc. ( First Western ), PMC Investment Corporation ( PMCIC ), Western Financial Capital Corporation ( Western Financial ), PMC Commercial Trust, Ltd. 1998-1 ( PMCT Trust ), PMC Funding Corp. ( PMC Funding ), PMC Asset Holding, LLC

( Asset Holding ), PMC Conduit, L.P. ( PMC Conduit ), PMC Properties, Inc. ( PMC Properties ) and four separate subsidiaries created in conjunction with the purchase of four hotel properties in 1999.

First Western is licensed as a small business lending company that originates loans through the SBA 7(a) Guaranteed Loan Program. PMCIC and Western Financial are licensed specialized small business investment companies under the Small Business Investment Act of 1958, as amended ( SBIA ). PMCT Trust was formed in conjunction with our 1998 structured loan financing transaction. PMC Funding, Asset Holding and PMC Conduit hold assets on our behalf. PMC Properties is the operator, through third party managers, of our limited service hospitality properties.

**PMC COMMERCIAL TRUST AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

*(Unaudited)*

In addition, we own subordinate financial interests in several non-consolidated special purpose entities (*i.e.*, retained interests in transferred assets ( Retained Interests )). These are PMC Capital, L.P. 1998-1 (the 1998 Partnership ), PMC Capital, L.P. 1999-1 (the 1999 Partnership ), PMC Joint Venture, L.P. 2000 (the 2000 Joint Venture ), PMC Joint Venture, L.P. 2001 (the 2001 Joint Venture ), PMC Joint Venture, L.P. 2002-1 (the 2002 Joint Venture ) and PMC Joint Venture, L.P. 2003 (the 2003 Joint Venture, and together with the 2000 Joint Venture, the 2001 Joint Venture and the 2002 Joint Venture, the Joint Ventures, and the Joint Ventures together with the 1998 Partnership and the 1999 Partnership, the QSPEs ) created in connection with structured loan sale transactions.

We account for our Retained Interests in accordance with Statement of Financial Accounting Standards ( SFAS ) No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities ( SFAS No. 140 ) and Emerging Issues Task Force Issue No. 99-20, Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets. While we are the servicer of the assets held by these QSPEs, we are required under the transaction documents to comply with strict servicing standards and are subject to the approval of the trustees and/or noteholders regarding any significant issues associated with the assets. As a result, we believe we have relinquished control of the assets sold to the QSPEs. Accordingly, the assets, liabilities, partners' capital and results of operations of the QSPEs are not included in our consolidated financial statements.

**Note 4. Reclassifications:**

Certain prior period amounts have been reclassified to conform to the current year presentation. These reclassifications had no effect on previously reported net income or total beneficiaries' equity.

**Note 5. Share-Based Compensation Plans:**

At March 31, 2006, we have options outstanding under share-based compensation plans. The 1993 Employee Share Option Plan and the Trust Manager Share Option Plan expired in December 2003; thus, no additional options will be issued under these two plans. The 2005 Equity Incentive Plan permits the grant of options to our employees, executive officers and Board of Trust Managers and restricted shares to our executive officers and Board of Trust Managers for up to 500,000 common shares. We use the fair value recognition provisions of SFAS No. 123R, Accounting for Stock-Based Compensation, to account for all awards granted, modified or settled.

We issued an aggregate of 9,060 restricted shares to executive officers and our Board of Trust Managers on June 11, 2005 at the then current market price of the shares at \$14.54. Compensation expense is being recognized over the vesting period. We recorded compensation expense of approximately \$17,000 during the three months ended March 31, 2006 for the vested portion of our restricted share issuance. As of March 31, 2006, there was approximately \$32,000 of total unrecognized compensation expense related to the unvested restricted shares which will be recognized over the next fourteen months.

**Note 6. Recently Issued Accounting Pronouncements:**

In May 2005, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 154 ( SFAS No. 154 ), Accounting Changes and Error Corrections which replaces Accounting Principles Board ( APB ) Opinion No. 20, Accounting Changes and SFAS No. 3, Reporting Accounting Changes in Interim Financial Statements An Amendment of APB



Opinion No. 28. SFAS No. 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. It establishes retroactive application, or the latest practicable date, as the required method for reporting a change in accounting principle and the reporting of a correction of an error. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The adoption of SFAS No. 154 did not have a material impact on our consolidated financial statements.

The FASB issued SFAS No. 155 ( SFAS No. 155 ), Accounting for Certain Hybrid Financial Instruments an amendment of FASB Statements No. 133 and 140 in February 2006. SFAS No. 155 (1) permits fair value remeasurement for hybrid financial instruments that contain an embedded derivative that would otherwise require bifurcation, (2) clarifies which interest-only strip receivables are not subject to the requirements of SFAS No. 133, (3) establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or hybrid financial instruments that