

MUNICIPAL MORTGAGE & EQUITY LLC

Form 10-Q

May 09, 2005

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-Q

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

For the quarterly period ended March 31, 2005

Commission File Number: 001-11981

MUNICIPAL MORTGAGE & EQUITY, LLC
(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

52-1449733

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

**621 E. Pratt Street, Suite 300
Baltimore, Maryland**

(Address of principal executive offices)

21202-3140

(Zip Code)

(443) 263-2900

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes No

The Registrant had 37,932,278 common shares outstanding as of May 2, 2005.

MUNICIPAL MORTGAGE & EQUITY, LLC
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Forward-Looking Information

This Quarterly Report on Form 10-Q contains forward-looking statements, which involve certain risks and uncertainties. Assumptions contained in various portions of this Quarterly Report on Form 10-Q involve judgments with respect to, among other things, future economic market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond the control of the Company. Although the Company believes that the assumptions underlying the forward-looking information included herein are reasonable, any of the assumptions could be inaccurate. Therefore, there can be no assurance that such forward-looking information will prove to be accurate. In light of the significant uncertainties inherent in forward-looking information, the inclusion of such information should not be regarded as a representation by the Company or any other person that the objectives and plans of the Company will be achieved.

PART I.
FINANCIAL INFORMATION

Item 1. Financial Statements.

MUNICIPAL MORTGAGE & EQUITY, LLC
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)
(unaudited)

	March 31, 2005	December 31, 2004
ASSETS		
Investment in tax-exempt bonds and interests in bond securitizations, net (Note 3)	\$ 1,353,049	\$ 1,275,748
Investment in taxable bonds, net (Note 3)	9,015	9,205
Loans receivable, net (Note 4)	637,525	593,968
Loans receivable held for sale (Note 4)	13,753	27,766
Investment in partnerships (Note 5)	758,313	827,273
Investments in derivative financial instruments (Note 6)	4,368	3,102
Cash and cash equivalents	57,805	92,881
Interest receivable	18,380	18,368
Restricted assets (Note 7)	89,940	72,805
Other assets	69,819	66,040
Land, building and equipment, net	179,143	182,773
Mortgage servicing rights, net	13,035	11,349
Goodwill	109,483	106,609
Other intangibles	23,854	22,443
Total assets	\$ 3,337,482	\$ 3,310,330
LIABILITIES AND SHAREHOLDERS EQUITY		
Notes payable (Note 8)	\$ 740,292	\$ 880,224
Mortgage notes payable (Note 8)	128,679	132,237
Short-term debt (Note 8)	488,048	413,157
Long-term debt (Note 8)	182,760	164,014
Subordinate debentures (Note 9)	134,000	84,000
Preferred shares subject to mandatory redemption	168,000	168,000
Tax credit equity guarantee liability (Note 10)	200,843	186,778
Investments in derivative financial instruments (Note 6)	2,949	4,923
Accounts payable and accrued expenses	14,714	35,003
Interest payable	17,607	19,266
Unearned revenue and other liabilities	88,139	74,176
Total liabilities	2,166,031	2,161,778
Commitments and contingencies (Note 11)		
Minority interest in subsidiary companies	377,550	404,586

Preferred shareholders equity in a subsidiary company, liquidation preference of \$73,000 at March 31, 2005 and December 31, 2004, respectively	71,031	71,031
Shareholders equity:		
Common shares, par value \$0 (42,046,099 shares authorized, including 37,955,251 shares issued and outstanding, and 63,196 deferred shares at March 31, 2005 and 39,471,099 shares authorized, including 35,179,884 shares issued and outstanding, and 58,114 deferred shares at December 31, 2004)	738,619	681,227
Less common shares held in treasury at cost (181,015 and 124,715 shares at March 31, 2005 and December 31, 2004, respectively)	(3,926)	(2,615)
Less unearned compensation (deferred shares)	(6,571)	(4,145)
Accumulated other comprehensive loss	(5,252)	(1,532)
Total shareholders equity	722,870	672,935
Total liabilities and shareholders equity	\$ 3,337,482	\$ 3,310,330

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

MUNICIPAL MORTGAGE & EQUITY, LLC
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except share and per share data)
(unaudited)

	For the three months ended March 31,	
	2005	2004
INCOME:		
Interest income		
Interest on bonds and interests in bond securitizations	\$ 23,085	\$ 19,502
Interest on loans	11,946	10,721
Interest on short-term investments	487	807
Total interest income	35,518	31,030
Fee income		
Syndication fees	4,608	3,751
Origination and brokerage fees	435	917
Guarantee fees	2,936	1,853
Asset management and advisory fees	5,686	6,166
Loan servicing fees	1,222	1,119
Other income	1,376	1,347
Total fee income	16,263	15,153
Net rental income	6,572	
Total income	58,353	46,183
EXPENSES:		
Interest expense	17,117	13,904
Interest expense on debentures and preferred shares (Note 9)	5,231	3,046
Salaries and benefits	17,849	15,584
General and administrative	9,170	3,698
Professional fees	1,878	1,494
Depreciation and amortization	3,794	1,939
Total expenses	55,039	39,665
Net (loss) gain on sale of loans	(286)	680
Net gain on sale of tax-exempt investments	914	192
Net gain on sale of investments in tax credit equity partnerships	841	2,435
Net gain (loss) on derivatives	2,888	(3,425)
Impairments and valuation allowances	(812)	(300)
	6,859	6,100

Income before income tax benefit, net income allocable to minority interest, net losses from equity investments in partnerships, and cumulative effect of a change in accounting principle

Income tax benefit	1,216	2,510
Net income allocable to minority interest	38,882	105
Net losses from equity investments in partnerships	(44,726)	(10,511)
Income (loss) before cumulative effect of a change in accounting principle	2,231	(1,796)
Cumulative effect of a change in accounting principle		520
Net income (loss)	\$ 2,231	\$ (1,276)

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

MUNICIPAL MORTGAGE & EQUITY, LLC
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (continued)
(in thousands, except share and per share data)
(unaudited)

Basic earnings per common share:

Earnings before cumulative effect of a change in accounting principle	\$	0.06	\$	(0.06)
Cumulative effect of a change in accounting principle				0.02

Basic earnings per common share	\$	0.06	\$	(0.04)
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Weighted average common shares outstanding	36,888,128	33,301,337
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Diluted earnings per common share:

Earnings before cumulative effect of a change in accounting principle	\$	0.06	\$	(0.06)
Cumulative effect of a change in accounting principle				0.02

Diluted earnings per common share	\$	0.06	\$	(0.04)
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Weighted average common shares outstanding	37,349,192	33,301,337
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The accompanying notes are an integral part of these financial statements.

MUNICIPAL MORTGAGE & EQUITY, LLC
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands)
(unaudited)

	For the three months ended	
	March 31,	
	2005	2004
Net income (loss)	\$ 2,231	\$ (1,276)
Other comprehensive loss:		
Unrealized gains (losses) on investments:		
Unrealized holding losses arising during the period	(2,806)	(4,204)
Reclassification adjustment for gains included in net income (loss)	(914)	(192)
Other comprehensive loss	(3,720)	(4,396)
Comprehensive loss	\$ (1,489)	\$ (5,672)

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

MUNICIPAL MORTGAGE & EQUITY, LLC
CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY
(in thousands, except share data)
(unaudited)

	Common Shares	Treasury Shares	Unearned Compensation	Accumulated Other Comprehensive Loss	Total
Balance, January 1, 2005	\$ 681,227	\$ (2,615)	\$ (4,145)	\$ (1,532)	\$ 672,935
Net income	2,231				2,231
Unrealized gains on investments, net of reclassifications				(3,720)	(3,720)
Distributions	(16,636)				(16,636)
Purchase of treasury shares		(1,311)			(1,311)
Options exercised	185				185
Issuance of common shares	64,927				64,927
Deferred shares issued under the Non-Employee Directors Share Plans	148				148
Deferred share grants	6,577		(6,577)		
Amortization of deferred compensation			4,151		4,151
Net tax expense from exercise of options and vesting of deferred shares	(40)				(40)
Balance, March 31, 2005	\$ 738,619	\$ (3,926)	\$ (6,571)	\$ (5,252)	\$ 722,870

SHARE ACTIVITY:	Common Shares	Treasury Shares
Balance, January 1, 2005	35,113,283	124,715
Options exercised	11,000	
Purchase of treasury shares	(56,300)	56,300
Issuance of common shares	2,575,000	
Issuance of common shares under employee share incentive plans	189,367	
Deferred shares issued under the Non-Employee Directors Share Plans	5,082	
Balance, March 31, 2005	37,837,432	181,015

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

MUNICIPAL MORTGAGE & EQUITY, LLC
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	For the three months ended March 31,	
	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	\$ 2,231	\$ (1,276)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Income allocated to subsidiary preferred shareholders	950	
Cumulative effect of a change in accounting principle		(520)
Net holding gains on trading securities	(3,240)	2,355
Impairments and valuation allowances related to investments	812	300
Amortization of guarantee liability	(2,099)	(1,075)
Net gain on sales	(1,469)	(3,307)
Loss from investments in partnerships	44,726	10,511
Minority interest income	(39,832)	(105)
Net amortization of premiums, discounts and fees on investments	(1,972)	(106)
Depreciation, accretion and amortization	4,419	2,936
Deferred income taxes	(1,429)	
Deferred share compensation expense	4,151	777
Common and deferred shares issued under the Non-Employee Directors Share Plans	148	56
Net change in assets and liabilities:		
Increase in interest receivable	(12)	(947)
Increase in other assets	(842)	(22,434)
Decrease in accounts payable, accrued expenses and other liabilities	(17,300)	(8,097)
(Increase) decrease in loans held for sale	(6,631)	32,168
Net cash (used in) provided by operating activities	(17,389)	11,236
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of bonds and interests in bond securitizations	(129,465)	(67,000)
Loan originations	(104,700)	(90,504)
Acquisition of MRC	(9,612)	
Purchases of property and equipment	(3,913)	(419)
Net investment in restricted assets	(17,321)	9,190
Principal payments received	82,851	47,465
Proceeds from the sale of investments	49,755	8,168
Distributions received from investments in partnerships	4,358	1,887
Net investments in partnerships	(99,303)	16,936
Net cash used in investing activities	(227,350)	(74,277)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings from credit facilities	194,142	280,438

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Repayment of credit facilities	(288,973)	(267,711)
Proceeds from tax credit syndication investors	114,447	2,364
Proceeds from short-term debt	132,010	2,495
Repayment of short-term debt	(57,119)	
Proceeds from long-term debt	69,077	1,140
Repayment of long-term debt	(331)	(4,438)
Purchase of treasury shares	(1,311)	
Issuance of common shares	64,927	52,466
Proceeds from stock options exercised	185	758
Distributions to common shares	(16,636)	(14,770)
Distributions to preferred shareholders in a subsidiary company	(755)	
Net cash provided by financing activities	209,663	52,742
Net decrease in cash and cash equivalents	(35,076)	(10,299)
Cash and cash equivalents at beginning of period	92,881	50,826
Cash and cash equivalents at end of period	\$ 57,805	\$ 40,527

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

MUNICIPAL MORTGAGE & EQUITY, LLC
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	For the three months ended March 31,	
	2005	2004
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Interest paid	\$ 23,307	\$ 24,492
Income taxes paid	\$ 467	\$ 1,146
Non-cash activity resulting from consolidation of VIEs under FIN 46:		
Investment in partnerships	\$ 144,496	\$ 1,382,800
Restricted assets	186	133,107
Other assets	209	
Land, building and equipment, net	5,256	
Notes payable	44,816	208,655
Mortgage notes payable	4,109	
Accounts payable, accrued expenses and other liabilities	3,394	32,138
Minority interest in subsidiary companies	97,828	1,274,533
Accumulated other comprehensive income		61

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

MUNICIPAL MORTGAGE & EQUITY, LLC
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

NOTE 1 BASIS OF PRESENTATION

Municipal Mortgage & Equity, LLC (**MuniMae** and, together with its subsidiaries, the **Company**) provides debt and equity financing to developers of multifamily housing and other real estate investments. The Company invests in tax-exempt bonds, or interests in bonds, issued by state and local governments or their agencies or authorities to finance multifamily housing developments. These tax-exempt bonds are not general obligations of state and local governments, or the agencies or authorities that issue the bonds. The multifamily housing developments, as well as the rents paid by the tenants, typically secure these investments. The Company also invests in other housing-related debt and equity investments, including equity investments in real estate operating partnerships; tax-exempt bonds, or interests in bonds, secured by student housing or assisted living developments; and tax-exempt bonds issued by community development districts to finance the development of community infrastructure supporting single-family housing, mixed use and commercial developments and secured by specific payments or assessments pledged by the local improvement district that issues the bonds (**CDD bonds**). Interest income derived from the majority of the Company's bond investments is exempt income for Federal income tax purposes. Real estate finance activities include the origination of, investment in and servicing of investments in multifamily housing, both for the Company's own account and on behalf of third parties. These activities generate income that is includable for Federal income tax purposes. The Company is also a tax credit syndicator. As a syndicator, the Company acquires and transfers to investors interests in partnerships that receive and distribute to investors low-income housing tax credits. The Company earns syndication fees on the placement of these interests with investors. The Company also earns fees for providing guarantees on certain tax credit equity funds and for managing the low-income housing tax credit equity funds it has syndicated.

MuniMae was organized in 1996 as a Delaware limited liability company. As a limited liability company, the Company combines many of the limited liability, governance and management characteristics of a corporation with the pass-through income features of a partnership. Since MuniMae is classified as a partnership for Federal income tax purposes, MuniMae is not itself subject to Federal and, in most cases, state and local income taxes. Instead, each shareholder must include his or her distributive share of MuniMae's income, deductions and credits on the shareholder's income tax return. Most of the Company's real estate finance and tax credit syndication activities are conducted through subsidiaries classified as corporations for Federal income tax purposes. These corporations do not have the pass-through income features of a partnership.

The condensed consolidated financial statements include the accounts of MuniMae, its wholly owned subsidiaries, its majority owned subsidiaries and variable interest entities (**VIEs**) where management determined that the Company was the primary beneficiary of the VIE. All significant intercompany balances and transactions have been eliminated.

The results of consolidated operations for the three-month period ended March 31, 2005 are not necessarily indicative of the results to be expected for the full year. The operating results from the Company's tax credit equity syndication business are expected to fluctuate based on seasonal patterns. The Company anticipates that its highest revenues from the tax credit business will occur in the third and fourth quarters. In addition, seasonality in tax-exempt bond originations is expected to result in higher volume in the second half of 2005.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (the **SEC**) and in the opinion of management contain all adjustments (consisting of only normal recurring accruals) necessary to present a fair statement of the results for the periods presented. These results have been determined on the basis of accounting principles and policies

discussed in Note 1 to the Company's Annual Report on Form 10-K for the year ended December 31, 2004 (the **Company's 2004 Form 10-K**). Certain information and footnote disclosures normally included in financial statements presented in accordance with generally accepted accounting principles in the United

States of America (**GAAP**) have been condensed or omitted. The accompanying financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's 2004 Form 10-K. Certain 2004 amounts have been reclassified to conform to the 2005 presentation with no effect on previously reported net income or shareholders' equity.

New Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (**FASB**) issued Statement of Financial Accounting Standards (**SFAS**) No. 123R, Share-Based Payment, a revision of SFAS No. 123, Accounting for Stock-Based Compensation and superseding APB Opinion No. 25, Accounting for Stock Issued to Employees (**FAS 123R**). FAS 123R requires the Company to expense grants made under the share option and employee share purchase plan programs. The cost will be recognized over the vesting period of the applicable share option or other share-based payment. In April 2005, the Securities and Exchange Commission approved a new rule that, for public companies, delays the effective date of SFAS 123R such that the Company must adopt it no later than January 1, 2006. Upon adoption of FAS 123R, amounts previously disclosed under SFAS No. 123 will be recorded in the consolidated income statement. The Company is continuing to evaluate the impact of this standard.

Share-Based Employee Compensation

The Company accounts for both the non-employee director share plans and the employee share incentive plans under the recognition and measurement principles of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees. No options were issued pursuant to the plans and, accordingly, no compensation expense was recognized for options issued under the plans for the three months ended March 31, 2005 and 2004. SFAS No. 148, Accounting for Stock-Based Compensation-Transition and Disclosure (**FAS 148**), requires the Company to make certain disclosures as if the compensation expense for the Company's plans had been determined based on the fair value on the date of grant for awards under those plans. The estimated fair values of options previously awarded were de minimis and would have no impact on the earnings per share calculation for the three months ended March 31, 2005 and 2004.

NOTE 2 ACQUISITIONS

On February 18, 2005, the Company purchased MONY Realty Capital, Inc. (**MRC**) from AXA Financial, Inc. (**AXA**) for a total purchase cost of \$10.5 million, comprised of cash paid to AXA of \$8.5 million, transaction costs of approximately \$1.1 million and liabilities assumed of approximately \$0.9 million. The Company has accounted for this acquisition as a purchase and has allocated the purchase cost to tangible and identified intangible assets based on their fair values. The excess purchase cost over the fair values of these assets has been recorded as goodwill. The Company allocated approximately \$2.9 million to tangible assets (primarily investments in partnerships, and receivables), \$4.8 million to identifiable intangibles (primarily management advisory contracts and mortgage servicing rights) and approximately \$2.8 million to goodwill. These purchase allocations could be revised in the future when finalization of pre- and post-acquisition activities with AXA is complete.

Additionally, as part of the purchase agreement, the Company committed to invest \$25.0 million in a real estate partnership in which MRC is already a general partner. This interest was acquired by the Company upon its acquisition of MRC. The Company is required to invest the remainder of the \$25.0 million commitment on or prior to the third anniversary of the closing date. As of the filing date, the Company had funded \$5.4 million of its commitment.

NOTE 3 INVESTMENT IN TAX-EXEMPT BONDS, TAXABLE BONDS AND INTERESTS IN BOND SECURITIZATIONS

The Company originates for its own account and for others investments in tax-exempt bonds. Tax-exempt bonds are issued by state and local government authorities to finance multifamily housing developments or other types of real estate including land infrastructure development. The multifamily bonds are secured primarily by non-recourse mortgage loans on affordable and market rate multifamily housing, while the land infrastructure bonds are secured by

sales tax liens and other assessments on the district.

The Company originates for its own account and for others investments in taxable bonds. Taxable bonds are issued by state and local government authorities to finance multifamily housing developments or land infrastructure development. The multifamily bonds are secured primarily by non-recourse mortgage loans on affordable and

market rate housing, while the land infrastructure bonds are secured by sales tax liens and other assessments on the district.

The Company invests in housing-related securities, including CDD bonds. The Company also invests in tax-exempt bonds, or interests in bonds, secured by student housing or assisted living developments.

The Company's sources of capital to fund these lending activities include proceeds from equity and debt offerings, securitizations, loans from warehousing facilities and lines of credit with banks, pension funds and finance companies and cash on hand. The Company earns interest income from its investment in tax-exempt bonds and taxable bonds. The Company also earns origination, construction administration and servicing fees through subsidiaries classified as corporations for Federal income tax purposes, for originating and servicing the bonds.

As of March 31, 2005 and December 31, 2004, the Company held tax-exempt bonds with a fair value of \$1,353.0 million and \$1,275.7 million and taxable bonds with a fair value of \$9.0 million and \$9.2 million, respectively. The following tables summarize the bonds by type.

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	Face Amount	March 31, 2005		Fair Value
		Amortized Cost	Unrealized Gain (Loss)	
<i>(in thousands)</i>				
Non-participating tax-exempt bonds	\$ 1,234,165	\$ 1,210,811	\$ (18,530)	\$ 1,192,281
Participating tax-exempt bonds	101,146	100,502	(6,286)	94,216
Subordinate non-participating tax-exempt bonds	6,558	6,379	(762)	5,617
Subordinate participating tax-exempt bonds	60,530	35,799	21,817	57,616
Interests in securitization trusts	4,698	4,687	(1,368)	3,319
Investment in taxable bonds	9,420	9,136	(121)	9,015
Total	\$ 1,416,517	\$ 1,367,314	\$ (5,250)	\$ 1,362,064