

MUNICIPAL MORTGAGE & EQUITY LLC

Form 10-Q

August 04, 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**

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2005
OR

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the period from _____ to _____
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 38,064,725 common shares outstanding as of August 1, 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)

| | June 30, 2005 | December 31, 2004 |
|---|---------------------|----------------------|
| ASSETS | | |
| Investment in tax-exempt bonds and interests in bond securitizations, net (Note 4) | \$ 1,354,108 | \$ 1,275,748 |
| Investment in taxable bonds, net (Note 4) | 16,389 | 9,205 |
| Loans receivable, net (Note 5) | 663,663 | 593,968 |
| Loans receivable held for sale (Note 5) | 715 | 27,766 |
| Investment in partnerships (Note 6) | 672,609 | 827,273 |
| Investments in derivative financial instruments (Note 7) | 2,381 | 3,102 |
| Cash and cash equivalents | 136,698 | 92,881 |
| Interest receivable | 20,002 | 18,368 |
| Restricted assets (Note 8) | 81,064 | 72,805 |
| Other assets | 82,966 | 66,040 |
| Land, building and equipment, net | 162,518 | 182,773 |
| Mortgage servicing rights, net | 13,309 | 11,349 |
| Goodwill | 107,561 | 106,609 |
| Other intangibles | 25,764 | 22,443 |
| Total assets | \$ 3,339,747 | \$ 3,310,330 |
| LIABILITIES AND SHAREHOLDERS EQUITY | | |
| Notes payable (Note 9) | \$ 740,183 | \$ 880,224 |
| Mortgage notes payable (Note 9) | 108,783 | 132,237 |
| Short-term debt (Note 9) | 490,215 | 413,157 |
| Long-term debt (Note 9) | 182,337 | 164,014 |
| Subordinate debentures (Note 10) | 172,750 | 84,000 |
| Preferred shares subject to mandatory redemption | 168,000 | 168,000 |
| Tax credit equity guarantee liability (Note 11) | 223,986 | 186,778 |
| Investments in derivative financial instruments (Note 7) | 3,246 | 4,923 |
| Accounts payable and accrued expenses | 21,173 | 35,003 |
| Interest payable | 16,172 | 19,266 |
| Unearned revenue and other liabilities | 90,256 | 74,176 |
| Total liabilities | \$ 2,217,101 | \$ 2,161,778 |
| Commitments and contingencies (Note 12) | | |
| Minority interest in subsidiary companies | 312,484 | 404,586 |
| Preferred shareholders equity in a subsidiary company, liquidation preference of \$73,000 at June 30, 2005 and December 31, 2004, respectively | 71,031 | 71,031 |

Shareholders equity (Note 13):

| | | |
|--|--------------------|--------------------|
| Common shares, par value \$0 (42,046,099 shares authorized, including 38,074,265 shares issued and outstanding, and 70,855 deferred shares at June 30, 2005 and 39,471,099 shares authorized, including 35,179,884 shares issued and outstanding, and 58,114 deferred shares at December 31, 2004) | 749,424 | 681,227 |
| Less common shares held in treasury at cost (181,015 and 124,715 shares at June 30, 2005 and December 31, 2004, respectively) | (3,987) | (2,615) |
| Less unearned compensation (deferred shares) | (7,539) | (4,145) |
| Accumulated other comprehensive income (loss) | 1,233 | (1,532) |
| Total shareholders equity | 739,131 | 672,935 |
| Total liabilities and shareholders equity | \$3,339,747 | \$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 June 30, | | For the six months ended June 30, | |
|--|---|---------------|--------------------------------------|---------------|
| | 2005 | 2004 | 2005 | 2004 |
| INCOME: | | | | |
| Interest income | | | | |
| Interest on bonds and interests in bond securitizations | \$ 24,361 | \$ 21,340 | \$ 47,446 | \$ 40,842 |
| Interest on loans | 11,665 | 11,388 | 23,611 | 22,109 |
| Interest on short-term investments | 994 | 1,859 | 1,481 | 2,666 |
| Total interest income | 37,020 | 34,587 | 72,538 | 65,617 |
| Fee income | | | | |
| Syndication fees | 4,424 | 4,190 | 9,032 | 7,941 |
| Origination and brokerage fees | 1,410 | 2,848 | 1,845 | 3,765 |
| Guarantee fees | 4,039 | 1,506 | 6,975 | 3,359 |
| Asset management and advisory fees | 5,344 | 1,967 | 11,030 | 8,133 |
| Loan servicing fees | 1,350 | 1,139 | 2,572 | 2,258 |
| Other income | 1,388 | 1,213 | 2,764 | 2,558 |
| Total fee income | 17,955 | 12,863 | 34,218 | 28,014 |
| Net rental income | 5,550 | 5,496 | 12,122 | 5,496 |
| Total income | 60,525 | 52,946 | 118,878 | 99,127 |
| EXPENSES: | | | | |
| Interest expense | 18,702 | 18,651 | 35,819 | 32,554 |
| Interest expense on debentures and preferred shares (Note 10) | 6,081 | 4,004 | 11,312 | 7,049 |
| Salaries and benefits | 19,839 | 20,460 | 37,688 | 36,044 |
| General and administrative | 7,546 | 6,654 | 16,716 | 10,352 |
| Professional fees | 3,466 | 2,731 | 5,344 | 4,225 |
| Depreciation and amortization | 3,937 | 3,936 | 7,731 | 5,875 |
| Total expenses | 59,571 | 56,436 | 114,610 | 96,099 |
| Net gain on sale of loans | 1,251 | 1,730 | 965 | 2,410 |
| Net gain on sale of tax-exempt investments | 5,159 | 1,013 | 6,073 | 1,205 |
| Net gain on sale of investments in tax credit equity partnerships | 5,723 | 379 | 6,564 | 2,814 |
| | 2,501 | | 2,501 | |

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| | | | | |
|---|-----------|-----------|-----------|----------|
| Net gain on deconsolidation of tax credit equity partnerships | | | | |
| Net gain on derivatives | 94 | 6,687 | 2,982 | 3,262 |
| Impairments and valuation allowances | (554) | (430) | (1,366) | (730) |
| Income before income tax (expense) benefit, net income allocable to minority interest, net losses from equity investments in partnerships, discontinued operations and cumulative effect of a change in accounting principle | 15,128 | 5,889 | 21,987 | 11,989 |
| Income tax (expense) benefit | (4,251) | (173) | (3,035) | 2,337 |
| Net income allocable to minority interest | 22,031 | 76,659 | 60,913 | 76,764 |
| Net losses from equity investments in partnerships | (9,330) | (71,224) | (54,056) | (81,735) |
| Income from continuing operations | 23,578 | 11,151 | 25,809 | 9,355 |
| Discontinued operations (Note 16) | | | | |
| Income before cumulative effect of a change in accounting principle | 23,578 | 11,151 | 25,809 | 9,355 |
| Cumulative effect of a change in accounting principle | | | | 520 |
| Net income | \$ 23,578 | \$ 11,151 | \$ 25,809 | \$ 9,875 |

(Continued)

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 | | For the six months ended | |
|---|----------------------------|------------|--------------------------|------------|
| | June 30, | | June 30, | |
| | 2005 | 2004 | 2005 | 2004 |
| Basic earnings per common share: | | | | |
| Income from continuing operations | \$ 0.62 | \$ 0.32 | \$ 0.69 | \$ 0.27 |
| Discontinued operations | | | | |
| Cumulative effect of a change in accounting principle | | | | 0.02 |
| Basic earnings per common share | \$ 0.62 | \$ 0.32 | \$ 0.69 | \$ 0.29 |
| Weighted average common shares outstanding | 37,919,842 | 34,800,580 | 37,404,006 | 34,047,243 |
| Diluted earnings per common share: | | | | |
| Income from continuing operations | \$ 0.61 | \$ 0.32 | \$ 0.68 | \$ 0.27 |
| Discontinued operations | | | | |
| Cumulative effect of a change in accounting principle | | | | 0.02 |
| Diluted earnings per common share | \$ 0.61 | \$ 0.32 | \$ 0.68 | \$ 0.29 |
| Weighted average common shares outstanding | 38,432,587 | 35,140,968 | 37,890,911 | 34,406,363 |

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 June 30, | | For the six months ended June 30, | |
|--|---|-----------------|--------------------------------------|-----------------|
| | 2005 | 2004 | 2005 | 2004 |
| Net income | \$ 23,578 | \$ 11,151 | \$ 25,809 | \$ 9,875 |
| Other comprehensive income (loss): | | | | |
| Unrealized gains (losses) on investments: | | | | |
| Unrealized holding gains (losses) arising during the period | 11,644 | (202) | 8,838 | (4,406) |
| Reclassification adjustment for gains included in net income | (5,159) | (1,013) | (6,073) | (1,205) |
| Other comprehensive income (loss) | 6,485 | (1,215) | 2,765 | (5,611) |
| Comprehensive income | \$ 30,063 | \$ 9,936 | \$ 28,574 | \$ 4,264 |

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 | Treasury | Unearned | Accumulated Other Comprehensive Income | Total |
|---|-----------|-----------|--------------|---|-----------|
| | Shares | Shares | Compensation | (Loss) | |
| Balance, January 1, 2005 | \$681,227 | \$(2,615) | \$(4,145) | \$ (1,532) | \$672,935 |
| Net income | 25,809 | | | | 25,809 |
| Unrealized gains on investments, net of reclassifications | | | | 2,765 | 2,765 |
| Distributions | (34,481) | | | | (34,481) |
| Purchase of treasury shares | | (1,372) | | | (1,372) |
| Options exercised | 1,155 | | | | 1,155 |
| Issuance of common shares | 65,935 | | | | 65,935 |
| Deferred shares issued under the Non-Employee Directors Share Plans | 278 | | | | 278 |
| Deferred share grants | 9,791 | | (9,791) | | |
| Amortization of deferred compensation | | | 6,397 | | 6,397 |
| Net tax expense from exercise of options and vesting of deferred shares | (290) | | | | (290) |
| Balance, June 30, 2005 | \$749,424 | \$(3,987) | \$(7,539) | \$ 1,233 | \$739,131 |

| | Common Shares | Treasury Shares |
|---|---------------|--------------------|
| SHARE ACTIVITY: | | |
| Balance, January 1, 2005 | 35,113,283 | 124,715 |
| Options exercised | 67,000 | |
| Purchase of treasury shares | (56,300) | 56,300 |
| Issuance of common shares | 2,575,000 | |
| Issuance of common shares under employee share incentive plans | 251,616 | |
| Deferred shares issued under the Non-Employee Directors Share Plans | 13,506 | |
| Balance, June 30, 2005 | 37,964,105 | 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 six months ended June 30, | |
|---|--------------------------------------|------------------|
| | 2005 | 2004 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | \$ 25,809 | \$ 9,875 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Income allocated to subsidiary preferred shareholders | 1,894 | |
| Cumulative effect of a change in accounting principle | | (520) |
| Net holding gains on trading securities | (1,823) | (5,498) |
| Impairments and valuation allowances related to investments | 1,366 | 730 |
| Amortization of guarantee liability | (4,722) | (2,149) |
| Net gain on sales | (13,602) | (6,429) |
| Net gain on deconsolidation of tax credit equity partnerships | (2,501) | |
| Loss from investments in partnerships | 54,056 | 81,735 |
| Minority interest income | (62,807) | (76,764) |
| Net amortization of premiums, discounts and fees on investments | (4,706) | 978 |
| Depreciation, accretion and amortization | 8,858 | 8,376 |
| Deferred income taxes | 2,442 | (2,527) |
| Deferred share compensation expense | 6,397 | 1,781 |
| Common and deferred shares issued under the Non-Employee Directors Share Plans | 278 | 104 |
| Net change in assets and liabilities: | | |
| Increase in interest receivable | (1,619) | (1,362) |
| Increase in other assets | (9,844) | (14,202) |
| Decrease (increase) in accounts payable, accrued expenses and other liabilities | (6,054) | 13,963 |
| Decrease in loans held for sale | 6,855 | 15,361 |
| Net cash provided by operating activities | 277 | 23,452 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchases of bonds and interests in bond securitizations | (194,253) | (182,928) |
| Loan originations | (210,128) | (164,956) |
| Acquisition of assets and businesses | (10,992) | |
| Purchases of property and equipment | (5,723) | (8,076) |
| Net investment in restricted assets | (27,720) | 10,484 |
| Principal payments received | 155,007 | 89,930 |
| Proceeds from the sale of investments | 118,761 | 38,479 |
| Distributions received from investments in partnerships | 23,147 | 3,694 |
| Net investments in partnerships | (170,935) | (132,383) |
| Net cash used in investing activities | (322,836) | (345,756) |

CASH FLOWS FROM FINANCING ACTIVITIES:

| | | |
|---|-------------------|------------------|
| Borrowings from credit facilities | 477,789 | 630,521 |
| Repayment of credit facilities | (552,368) | (477,502) |
| Proceeds from tax credit syndication investors | 227,292 | 107,708 |
| Proceeds from short-term debt | 221,055 | 38,200 |
| Repayment of short-term debt | (143,997) | (588) |
| Proceeds from long-term debt | 107,827 | 61,140 |
| Repayment of long-term debt | (754) | (11,242) |
| Purchase of treasury shares | (1,372) | |
| Issuance of common shares | 65,935 | 52,482 |
| Proceeds from stock options exercised | 1,155 | 1,410 |
| Distributions to common shares | (34,481) | (30,689) |
| Distributions to preferred shareholders in a subsidiary company | (1,705) | |
| Net cash provided by financing activities | 366,376 | 371,440 |
| Net increase in cash and cash equivalents | 43,817 | 49,136 |
| Cash and cash equivalents at beginning of period | 92,881 | 50,826 |
| Cash and cash equivalents at end of period | \$ 136,698 | \$ 99,962 |

*(Continued)**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 six months ended | |
|--|--------------------------|-----------|
| | June 30, | |
| | 2005 | 2004 |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION: | | |
| Interest paid | \$ 48,355 | \$ 38,871 |
| Income taxes paid | \$ 576 | \$ 3 |
| Non-cash activity related to VIEs under FIN 46: | | |
| Loans receivable | \$ 8,812 | \$ |
| Investment in partnerships | 225,177 | 1,271,457 |
| Restricted assets | 19,461 | 134,228 |
| Other assets | 1,165 | 21,150 |
| Land, building and equipment, net | 21,598 | 166,360 |
| Notes payable | 65,922 | 208,655 |
| Mortgage notes payable | 23,476 | 123,900 |
| Accounts payable, accrued expenses and other liabilities | 5,640 | 35,277 |
| Minority interest in subsidiary companies | 181,175 | 1,182,482 |
| 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, and sourcing, underwriting, structuring and managing of commercial real estate investments, 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- and six-month periods ended June 30, 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 SEC approved a new rule for public companies that 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.

In June 2005, the FASB ratified the consensus in EITF Issue No. 04-5, Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights (**Issue 04-5**), which provides guidance in determining whether a general partner controls a limited partnership. To promote consistency in applying this guidance to corporate entities and those entities that hold real estate:

the EITF amended Issue No. 96-16, Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Interest Shareholder or Shareholders Have Certain Approval or Veto Rights (Issue 96-16), and

the FASB staff issued FSP No. SOP 78-9-1, which amends AICPA Statement of Position 78-9, Accounting for Investments in Real Estate Ventures, to reflect the consensus reached in Issue 04-5.

The effective date for applying the guidance in Issue 04-5 and FSP SOP 78-9-1 is (1) June 29, 2005, for all new limited partnerships and existing limited partnerships for which the partnership agreements are modified and (2) no later than the beginning of the first reporting period in fiscal years beginning after December 15, 2005, for all other limited partnerships. Thus far, the impact of Issue 04-5 has had no effect on the Company's financial statements. The Company will continue to evaluate the impact of Issue 04-5 throughout the remainder of 2005.

NOTE 2 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 six months ended June 30, 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 six months ended June 30, 2005 and 2004.

NOTE 3 ACQUISITIONS

On February 18, 2005, the Company purchased MONY Realty Capital, Inc. (**MRC**) from AXA Financial, Inc. (**AXA**) for a total purchase cost of \$10.9 million comprised of cash paid to AXA of \$8.5 million, transaction costs of approximately \$1.4 million and liabilities assumed of approximately \$1.0 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), \$7.0 million to identifiable intangibles (primarily management advisory contracts, mortgage servicing rights and customer relationship value) and approximately \$0.9 million to goodwill.

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 June 30, 2005, the Company had funded \$7.9 million of its

commitment.

NOTE 4 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 and taxable bonds. Tax-exempt and taxable bonds are issued by state and local government authorities to finance multifamily housing developments or other types of real estate, including land infrastructure development (CDD Bonds). 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 property tax or sales tax liens and other assessments on the district. 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 June 30, 2005 and December 31, 2004, the Company held tax-exempt bonds with a fair value of \$1,354.1 million and \$1,275.7 million and taxable bonds with a fair value of \$16.4 million and \$9.2 million, respectively. The following tables summarize the bonds by type.

| (in thousands) | June 30, 2005 | | | | |
|--|---------------------|---------------------|------------------|-------------------|---------------------|
| | Face Amount | Amortized Cost | Unrealized Gain | Unrealized Loss | Fair Value |
| Non-participating tax-exempt bonds | \$ 1,229,186 | \$ 1,207,070 | \$ 33,040 | \$(47,453) | \$ 1,192,657 |
| Participating tax-exempt bonds | 101,092 | 100,473 | 5,643 | (12,207) | 93,909 |
| Subordinate non-participating tax-exempt bonds | 6,555 | 6,377 | 208 | (1,021) | 5,564 |
| Subordinate participating tax-exempt bonds | 60,530 | 35,799 | 23,763 | (358) | 59,204 |
| Interests in securitization trusts | 3,183 | 3,176 | | (402) | 2,774 |
| Investment in taxable bonds | 16,650 | 16,367 | 25 | (3) | 16,389 |
| Total | \$ 1,417,196 | \$ 1,369,262 | \$ 62,679 | \$(61,444) | \$ 1,370,497 |

| (in thousands) | December 31, 2004 | | | | |
|--|---------------------|---------------------|------------------|-------------------|---------------------|
| | Face Amount | Amortized Cost | Unrealized Gain | Unrealized Loss | Fair Value |
| Non-participating tax-exempt bonds | \$ 1,154,541 | \$ 1,129,842 | \$ 31,071 | \$(44,156) | \$ 1,116,757 |
| Participating tax-exempt bonds | 101,234 | 100,565 | 5,280 | (10,923) | 94,922 |
| Subordinate non-participating tax-exempt bonds | 6,562 | 6,383 | 184 | (936) | 5,631 |
| Subordinate participating tax-exempt bonds | 60,530 | 35,799 | 20,310 | (1,334) | 54,775 |
| Interests in securitization trusts | 4,698 | 4,687 | 36 | (1,060) | 3,663 |
| Investment in taxable bonds | 9,489 | 9,205 | | | 9,205 |
| Total | \$ 1,337,054 | \$ 1,286,481 | \$ 56,881 | \$(58,409) | \$ 1,284,953 |

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During the six months ended June 30, 2005, the Company invested in tax-exempt bonds with a face amount of \$187.8 million for \$187.0 million. Of the total face amount of \$187.8 million, \$121.0 million represents the Company's new primary investments (bonds which the Company originated) and \$66.8 million reflects new secondary market investments (previously issued securities purchased from third parties).

The Company structures some tax-exempt bonds so that the borrower makes draws on the bonds throughout the construction period (**draw down bonds**). In the year these bonds are originated, the total draws for the year are reported as new primary investments. The Company originated a face amount of \$35.7 million in new draw down bonds during the six months ended June 30, 2005. The Company also funded an additional \$33.4 million of existing tax-exempt draw down bonds with a face amount of \$33.4 million for the six months ended June 30, 2005.

Thirteen tax-exempt bonds with an amortized cost of \$112.7 million were redeemed or sold during the six months ended June 30, 2005. The Company recognized a gain of \$6.1 million related to these bonds. Of the \$112.7 million, five bonds that were in a bond securitization and four bonds that were wholly owned with an amortized cost of \$92.9 million and \$1.2 million, respectively, were redeemed during the six months ended June 30, 2005, resulting in a gain totaling \$4.5 million. Two bonds that were in a bond securitization, one bond that was wholly owned and one senior interest in a bond securitization with an amortized cost of \$13.0 million, \$4.1 million and \$1.5 million, respectively, were sold during the six months ended June 30, 2005, resulting in a gain totaling \$1.6 million.

In order to facilitate the securitization of certain assets at higher leverage ratios than otherwise would be available to the Company without the posting of additional collateral, the Company has pledged additional bonds to various pools that act as collateral for senior interests in certain securitization trusts. From time to time, the Company pledges bonds as collateral for letters of credit, lines of credit, warehouse lending arrangements, other investments and derivative agreements. In addition, at times the Company pledges collateral when providing a guarantee in connection with the syndication of tax credit equity funds. At June 30, 2005 and December 31, 2004, the total carrying amount of the tax-exempt bonds pledged as collateral was \$578.4 million and \$537.0 million, respectively. At June 30, 2005 and December 31, 2004, the total carrying amount of taxable bonds pledged as collateral was \$14.7 million and \$0, respectively.

During the six months ended June 30, 2005, the Company recorded an other than temporary impairment of \$0.3 million on one tax-exempt bond with a face amount of \$1.5 million. During the six months ended June 30, 2004, the Company recorded an other than temporary impairment of \$0.7 million on three tax-exempt bonds with an aggregate face amount of \$17.8 million.

NOTE 5 LOANS RECEIVABLE

The Company's loans receivable and loans receivable held for sale consist primarily of construction loans, permanent loans, taxable supplemental loans and other taxable loans. The following table summarizes loans receivable by loan type at June 30, 2005 and December 31, 2004.

| (in thousands) | June 30, 2005 | December 31, 2004 |
|---------------------------|------------------|----------------------|
| Loan Type: | | |
| Construction loans | \$504,263 | \$503,745 |
| Taxable permanent loans | 715 | 27,766 |
| Supplemental loans | 75,056 | 62,079 |
| Other taxable loans | 87,576 | 31,104 |
| | 667,610 | 624,694 |
| Allowance for loan losses | (3,232) | (2,960) |
| Total | \$664,378 | \$621,734 |

Note: Supplemental loans include pre-development loans, bridge loans and other loans.

The Company had loans receivable held for sale of \$0.7 million and \$27.8 million at June 30, 2005 and December 31, 2004, respectively. These loans committed for sale are sold to Federal National Mortgage Association (**Fannie Mae**), Government National Mortgage Association (**GNMA**) and third party conduit lenders. Due to the short time the Company holds these loans, carrying value approximates fair value.

The Company pledges loans as collateral for the Company's notes payable, warehouse lending arrangements and line of credit borrowings. In addition, in order to facilitate the securitization of certain assets at higher leverage ratios than otherwise available to the Company without the posting of additional collateral, the Company has pledged additional taxable loans to a pool that acts as collateral for senior interests in certain securitization trusts and credit enhancement facilities. At June 30, 2005 and December 31, 2004, the total carrying amount of the loans receivable pledged as collateral was \$526.5 million and \$548.0 million, respectively.

The Company places delinquent loans on non-accrual status for financial reporting purposes when collection of interest is in doubt, which is generally after 90 days of non-payment. At June 30, 2005 and December 31, 2004, there were \$39.2 million and \$77.4 million (face value), respectively, of loans on non-accrual status.

NOTE 6 INVESTMENT IN PARTNERSHIPS,

The Company's investments in partnerships consist of equity interests in real estate operating partnerships. The Company's investments in partnerships are accounted for using the equity method. The following table summarizes investment in partnerships by major category at June 30, 2005 and December 31, 2004:

| (in thousands) | June 30, 2005 | December 31, 2004 |
|--|------------------|----------------------|
| Non-guaranteed tax credit equity funds: | | |
| Investment in real estate operating partnerships (1) | \$402,276 | \$563,310 |
| Guaranteed tax credit equity funds: | | |
| Investment in real estate operating partnerships (2) | 151,337 | 149,078 |
| Investment in real estate operating partnerships warehousing (3) | 42,733 | 43,873 |
| Investment in CAPREIT (4) | 64,619 | 70,351 |
| Investments in real estate operating partnerships MRC (5) | 9,979 | |
| Other investments in partnerships | 1,665 | 661 |
| | \$672,609 | \$827,273 |

(1) As a result of Financial Interpretation No. 46 (Revised) (**FIN 46R**), the Company must include on its balance sheet investments by certain non-guaranteed tax credit equity funds. These funds invest in limited partnership interests in real estate operating partnerships (**Project Partnerships**).

(2) These investments are real estate operating partnerships owned by tax credit equity funds where the Company provides a guarantee or

otherwise has continuing involvement in the underlying assets of the fund. As a result of the guarantee, the Company includes the assets of the funds in its consolidated balance sheets until such time as the Company's guarantee expires.

- (3) The Company acquires, through limited partnership interests, equity interests, which typically represent a 99.0% interest in properties expected to earn tax credits. When the Company has a sufficient number of such limited partnership interests and has identified tax credit investors, it transfers those interests to a tax credit equity fund for the investors benefit. The Company typically owns these partnership interests for three to nine months before they are transferred to a tax credit equity fund.
- (4) The Company makes equity investments in income-producing

real estate
partnerships in
joint ventures with
CAPREIT, Inc.
and its affiliates.

- (5) The Company
makes equity
investments in
income-producing
real estate
partnerships
through MRC and
its affiliates.

NOTE 7 INVESTMENTS IN DERIVATIVE FINANCIAL INSTRUMENTS

At June 30, 2005 and December 31, 2004, the Company's investments in derivative financial instruments consisted of interest rate swaps, put option contracts and total return swaps.

In March 2005, the Company entered into a contractual arrangement whereby the counterparty to the arrangement will purchase tax-exempt bonds from the Company or a third party and hold the bonds for a minimum of 30 days. The Company will have the option to bid for the purchase of the bonds at the time of sale by the counterparty. Regardless of whether the bonds are purchased by the Company or not, the Company will pay to the counterparty or receive from the counterparty amounts for any declines or increases in the bonds' market values from the date of purchase to the date of swap termination. The arrangement is considered a derivative transaction and is included in the balance of the total return swaps in the table below. The total maximum notional amount of the swap is \$50.0 million, based on the underlying value of the bonds held by the counterparty. The Company will receive a 1.50% annual fee on the outstanding notional amount of the swap. During the term of the swap, the Company is required to post collateral equal to the amount by which the purchase price of the bond or bonds subject to the swap exceeds the quoted market value by more than \$1.0 million. The arrangement has a maturity date of December 31, 2005. As of June 30, 2005, the Company had three swaps outstanding under this arrangement with a total notional amount of \$15.7 million.

In June 2005, the Company terminated interest rate swap contracts with a total notional amount of \$35.0 million. The Company recorded a net gain of \$1.5 million on the termination of these interest rate swaps. In addition, the Company in conjunction with a new non-revolving term financing facility (see Note 9) entered into a new interest rate swap contract with a total notional amount of \$18.4 million and an effective date in July 2005. The total notional amount of this contract is expected to increase to \$22.0 million in the third quarter of 2005. In addition to the above-mentioned interest rate swaps, the Company entered into two other interest rate swaps with a total notional amount of \$16.9 million in February of 2005.

The following table provides certain information with respect to the derivative financial instruments held by the Company at June 30, 2005 and December 31, 2004:

| | June 30, 2005 | | | December 31, 2004 | | |
|---|---------------|----------------|-----------------|-------------------|----------------|-----------------|
| | Notional | Fair Value (1) | | Notional | Fair Value (1) | |
| (in thousands) | Amount | Assets | Liabilities (2) | Amount | Assets | Liabilities (2) |
| Interest rate swap agreements (3) | \$337,850 | \$2,148 | \$(3,122) | \$286,015 | \$3,102 | \$(4,878) |
| Total return swaps (4) | 38,870 | 233 | (82) | 38,200 | | |
| Put option agreements (5) | 99,930 | | | 105,610 | | (45) |
| Loan commitments (6) | 43,449 | | (42) | | | |
| Total investments in derivative financial instruments | | \$2,381 | \$(3,246) | | \$3,102 | \$(4,923) |

(1) The amounts disclosed represent the net fair values of all the Company's derivatives at the reporting date.

(2) The aggregate negative fair value of the investments is included in liabilities for financial reporting purposes. The negative fair value of these investments is considered temporary and is not indicative of the future earnings on these investments.

(3)

For the interest rate swap agreements, notional amount represents the total amount of the Company's interest rate swap contracts (\$337,850 as of June 30, 2005 and \$320,975 as of December 31, 2004) less the total amount of the Company's reverse interest rate swap contracts (\$0 as of June 30, 2005 and \$34,960 as of December 31, 2004).

- (4) For the total return swaps, the notional amount represents the total amount of the Company's total return swap contracts.
- (5) For put option agreements, the notional amount represents the Company's aggregate obligation under the put option agreements.
- (6) Loan commitments represent agreements to take out construction loans originated

by the
Company.

NOTE 8 RESTRICTED ASSETS

Restricted assets includes cash and cash equivalents summarized by major category in the table below at June 30, 2005 and December 31, 2004:

| (in thousands) | June 30, 2005 | December 31, 2004 |
|--|------------------|-------------------------|
| Tax credit equity fund cash (1) | \$51,762 | \$49,069 |
| Margin call deposits (2) | 881 | 452 |
| Collateral for securitization programs (3) | 17,000 | 17,000 |
| Other cash collateral (4) | 11,421 | 6,284 |
| | \$81,064 | \$72,805 |

(1) Under the financing method of accounting for guaranteed tax credit equity funds and due to the consolidation of certain other funds in accordance with FIN 46R, the Company reports the restricted cash of the funds in the Company's consolidated balance sheet. The cash is to be used primarily for investments by the consolidated funds into partnerships and other approved uses as set out in the funds partnership agreements.

(2)

Under the terms of the Company's interest rate swap agreements with counterparties, the Company is required to maintain cash deposits (**margin call deposits**). The margin call deposit requirements are specific to each counterparty. The Company must make margin call deposits when the total fair value of the Company's outstanding swap obligations to any one counterparty is, in most cases, greater than \$1.0 million.

- (3) In order to facilitate the securitization of certain assets at higher leverage ratios than otherwise available to the Company without the posting of additional collateral, the Company has pledged additional bonds to a pool that

acts as collateral for senior interests in certain securitization trusts. From time to time, the Company may also post cash or cash equivalents to this pool.

- (4) From time to time, the Company may elect to pledge collateral in connection with guarantees, first loss positions and leases or on behalf of its customers in order to facilitate credit and other collateral requirements. Collateral posted on behalf of its customers is considered temporary and the Company expects to be fully reimbursed.

NOTE 9 NOTES PAYABLE AND DEBT

The Company's notes payable consist primarily of notes payable and advances under line of credit arrangements which are used to: (1) finance lending activities; (2) finance working capital needs; and (3) warehouse real estate operating partnerships before they are placed into tax credit equity funds. Notes payable also includes factored and mortgage notes payable reflected on the Company's balance sheet as a result of consolidating certain tax credit equity funds pursuant to FIN 46R. The factored notes payable are obligations of the limited partners (investors) of the tax-credit funds and collateralized by the investors' subscription receivables. The factored notes payable are non-recourse and not guaranteed by the Company. The mortgage notes payable are obligations of Project Partnerships, in which the Company is the general partner, and are non-recourse and not guaranteed by the Company. The Company's short- and long-term debt relates to securitization transactions and other financing transactions that the Company has recorded as borrowings. The following table summarizes notes payable and debt at June 30, 2005 and December 31, 2004:

| (in thousands) | Total of Facilities (a) | June 30, 2005 | December 31, 2004 |
|--|----------------------------|--------------------|----------------------|
| Short-term notes payable | N/A | \$ 171,867 | \$ 193,311 |
| Lines of credit | \$437,000(b) | 237,181 | 307,306 |
| Short-term debt | N/A | 490,215 | 413,157 |
| Total short-term notes payable and debt | | 899,263 | 913,774 |
| Long-term notes payable | \$ N/A | 129,875 | 173,440 |
| Lines of credit | 272,000 | 85,849 | 14,080 |
| Long-term debt | N/A | 182,337 | 164,014 |
| Total long-term notes payable and debt | | 398,061 | 351,534 |
| Factored notes payable | | 115,411 | 192,087 |
| Mortgage notes payable | | 108,783 | 132,237 |
| Total notes payable and debt | | \$1,521,518 | \$1,589,632 |

(a) As of June 30, 2005.

(b) \$39.0 million of these facilities are reserved for letters of credit.

In April 2005, the Company amended its Warehousing Credit and Security Agreement with Residential Funding Corporation. The amendment provides, among other things, that: the agency portion of the facility that was scheduled to expire on April 30, 2005 is extended until July 31, 2005; the non-utilization fee and compensating balance requirements are eliminated; and the limit for the agency portion of the facility is \$75.0 million, with the remaining funding limited to \$125.0 million.

During the second quarter of 2005, the Company entered into a new term financing facility of up to \$22.0 million. The facility is secured by certain taxable bonds and has a maturity date of May 1, 2010. Interest accrues at London Interbank Offer Rate (**LIBOR**) plus a spread. In connection with this facility, the Company entered into certain interest rate swap agreements (see Note 7).

Covenant Compliance

Under the terms of the various credit facilities, the Company is required to comply with covenants including net worth, interest coverage, leverage, collateral and other terms and conditions.

As of June 30, 2005, the Company was in compliance with the covenants in its credit facilities.

NOTE 10 SUBORDINATE DEBENTURES

A consolidated indirect wholly owned subsidiary of the Company, MMA Financial Holdings, Inc. (**MFH**), formed MFH Capital Trust II (**MFH Trust II**) and MFH Capital Trust III (**MFH Trust III**) in 2005 as special purpose financing entities. MFH Trust II and MFH Trust III are unconsolidated entities. On March 15, 2005, MFH Trust II sold to qualified institutional investors \$50.0 million in 8.05% Trust Preferred Securities having a liquidation amount of \$1,000 per Trust Preferred Security. On June 28, 2005, MFH Trust III sold to qualified institutional investors \$38.8 million in 7.62% Trust Preferred Securities having a liquidation amount of \$1,000 per Trust Preferred Security. MFH Trust II and MFH Trust III used the proceeds from the offerings to purchase Junior Subordinated Debentures (the **Debentures**) issued by MFH. The Debentures have substantially the same economic terms as the Trust Preferred Securities. MFH Trust II and MFH Trust III can make distributions to holders of the Trust Preferred Securities only if MFH makes payments on the Debentures. The Debentures are unsecured obligations and are subordinate to all of MFH's existing and future senior debt.

The Trust Preferred Securities issued by MFH Trust II and MFH Trust III are guaranteed by MFH and MuniMae. The Trust Preferred Securities issued by MFH Trust II bear interest at an annual rate of 8.05% through the interest payment date in March 2015, to be adjusted thereafter to a variable rate, reset quarterly, equal to the 90-day LIBOR plus 3.30% per annum of the liquidation preference of the Trust Preferred Securities and may be redeemed in whole or in part beginning on March 30, 2010. The Trust Preferred Securities issued by MFH Trust III bear interest at an annual rate of 7.62% through the interest payment date in June 2015, to be adjusted thereafter to a variable rate, reset quarterly, equal to the LIBOR plus 3.30% per annum of the liquidation preference of the Trust Preferred Securities and may be redeemed in whole or in part beginning on July 31, 2010. Cash distributions on the Trust Preferred Securities are paid quarterly. MFH used the March 15, 2005, offering net proceeds from the Debentures to repay a portion of a loan from an affiliate and other indebtedness of MFH and its affiliates, and for general corporate purposes. MFH loaned the June 28, 2005, net proceeds from the Debentures to an affiliate, which in turn used the proceeds towards the acquisition of Glaser Financial Group, Inc. (see Note 17 Subsequent Events). MFH Trust II and MFH Trust III must redeem the Trust Preferred Securities when and to the extent the Debentures are paid at maturity or earlier redeemed. The Debentures are included in the accompanying condensed consolidated balance sheet as a long-term liability at the liquidation preference value of \$88.8 million. In addition, net offering costs of \$2.9 million related to the Trust Preferred Securities are recorded as debt issuance costs and included in other assets in the accompanying condensed consolidated balance sheet. The offering costs paid by MFH are amortized to interest expense in the accompanying condensed consolidated income statement over a 30-year period based on the call option of the preferred shares.

NOTE 11 TAX CREDIT EQUITY GUARANTEE LIABILITY

As part of the acquisition of the HCI business (**HCI**) of Lend Lease Corporation Limited (**Lend Lease**), the Company provided guarantees to Lend Lease related to certain tax credit equity syndication funds where Lend Lease is providing a guarantee to investors or a third party. In addition, subsequent to the acquisition of HCI, the Company has established new guaranteed tax credit equity funds whereby the Company provides a guarantee to a third party or investors. The following table shows the changes in the tax credit equity guarantee liability:

(in thousands)

| | |
|---|------------|
| Balance at January 1, 2005 | \$ 186,778 |
| Amortization | (4,722) |
| Expiration of guarantees | (33,482) |
| Limited partners' capital contributions | 75,412 |
| Balance at June 30, 2005 | \$ 223,986 |

NOTE 12 GUARANTEES, COMMITMENTS AND CONTINGENCIES

The Company's maximum exposure under its guarantee obligations may not be indicative of the likelihood of the expected loss under the guarantees. The following table summarizes the Company's guarantees by type at June 30, 2005.

| (in millions) | | | June 30, 2005 | |
|---|------|------------------|-----------------|--|
| Guarantee | Note | Maximum Exposure | Carrying Amount | Supporting Collateral |
| Loss-sharing agreements with Fannie Mae, GNMA and HUD | (1) | \$ 195.3 | \$ | \$4.0 million letter of credit pledged |
| Bank line of credit guarantees | | | | \$200.2 million of investment in partnership, loans receivable, tax-exempt and taxable bonds |
| Tax credit-related guarantees | (2) | 173.2 | 173.2 | \$48.3 million of cash, tax-exempt bonds, loans receivable and letters of credit |
| Other financial/payment guarantees | (3) | 513.8 | 232.3 | \$542.9 million of cash, equity and tax-exempt bonds |
| Put options | (4) | 471.0 | 312.4 | \$60.3 million of tax-exempt bonds |
| Letter of credit guarantees | (5) | 69.6 | | \$11.6 million of cash and loans receivable |
| Indemnification contracts | (6) | 131.4 | 65.0 | None |
| Trust preferred guarantees | (7) | 77.2 | 26.1 | None |
| | (8) | 174.1 | 174.1 | None |
| | | \$1,805.6 | \$983.1 | |

(1) As a Fannie Mae DUS™ lender and GNMA loan servicer, the Company may share in losses relating to underperforming real estate mortgage loans delivered to Fannie Mae and GNMA. More specifically, if the borrower fails to make a payment of principal, interest, taxes or insurance premiums on a DUS loan

originated by the Company and sold to Fannie Mae, the Company may be required to make servicing advances to Fannie Mae.

Also, the Company may participate in a deficiency after foreclosure on Fannie Mae DUS and GNMA loans. The term of the loss sharing agreement is based on the contractual requirements of the underlying loans delivered to Fannie Mae and GNMA, which varies to a maximum of 40 years.

- (2) The Company provides payment or performance guarantees for certain borrowings under line of credit facilities. The amount outstanding under these lines of credit was \$172.0 million at June 30, 2005. This amount is included in notes payable in the Company's consolidated

balance sheet.

(3) The Company acquires and sells interests in partnerships that provide low-income housing tax credits for investors. In conjunction with the sale of these partnership interests, the Company may provide performance guarantees on the underlying properties owned by the partnerships or guarantees to the fund investors. These guarantees have various expirations to a maximum term of 20 years.

(4) The Company has entered into arrangements that require the Company to make payments in the event a specified third party fails to perform on its financial obligation. The Company typically provides these guarantees in conjunction with the sale of an asset to a third party or the

Company's investment in equity ventures. The term of the guarantee varies based on loan payoff schedules or Company divestitures.

- (5) The Company has entered into put option agreements with counterparties whereby the counterparty has the right to sell to the Company, and the Company has the obligation to buy, an underlying investment at a specified price. These put option agreements expire at various dates through June 2010.
- (6) The Company provides a guarantee of the repayment on losses incurred under letters of credit issued by third parties or to provide substitute letters of credit at a predetermined future date. In addition, the Company may provide a payment guarantee for certain assets in securitization

programs. These guarantees expire at various dates through September 2007.

- (7) The Company has entered into indemnification contracts, which require the guarantor to make payments to the guaranteed party based on changes in an underlying investment that is related to an asset or liability of the guaranteed party. These agreements typically require the Company to reimburse the guaranteed party for legal and other costs in the event of an adverse judgment in a lawsuit or the imposition of additional taxes due to a change in the tax law or an adverse interpretation of the tax law. The term of the indemnification varies based on the underlying program life, loan payoffs, or Company divestitures. Based on the terms of the underlying contracts, the

maximum exposure amount only includes amounts that can be reasonably estimated at this time. The actual exposure amount could vary significantly.

- (8) The Company provides a payment guarantee of the underlying trust preferred securities issued. The guarantee obligation is unsecured and subordinated to the Company's existing and future debt and liabilities except for debt and liabilities which by their terms are specifically subordinated to the guarantee obligations and the rights of the holders of various classes of existing and future preferred shares of the Company.

NOTE 13 SHAREHOLDERS EQUITY

Equity Offering

In February 2005, the Company sold to the public approximately 2.6 million common shares at a price of \$26.51 per share. Net proceeds on the 2.6 million shares approximated \$64.9 million. The net proceeds from this offering were used for general corporate purposes, including funding of new investments, paying down debt and working capital.

Share Repurchase Program

During the first quarter of 2005, the Company purchased 56,300 common shares at an aggregate cost of \$1.3 million under a share repurchase program previously approved by the Board of Directors.

Distributions

On January 21, 2005, the Board of Directors declared a distribution of \$0.4725 for the three months ended December 31, 2004 to common shareholders of record on January 31, 2005. The payment date was February 11, 2005. On April 21, 2005, the Board of Directors declared a distribution of \$0.4775 for the three months ended March 31, 2005 to common shareholders of record on May 2, 2005. The payment date was May 13, 2005.

Earnings per Share

The following tables reconcile the numerators and denominators in the basic and diluted earnings per share (**EPS**) calculations for common shares for the three and six months ended June 30, 2005 and 2004. The effect of all potentially dilutive securities was included in the calculation for June 30, 2005 and 2004. The computation of diluted EPS for the three and six months ended June 30, 2005 and 2004 excluded 39,000 and 67,000 options to purchase common shares, respectively.

Municipal Mortgage & Equity, LLC
RECONCILIATION OF BASIC AND DILUTED EPS

(in thousands, except share and per share data)

(unaudited)

| | For the three months ended June 30, 2005 | | | For the three months ended June 30, 2004 | | |
|--|---|---------------|---------|---|---------------|---------|
| | Income | Shares | Per | Income | Shares | Per |
| | (Numerator) | (Denominator) | Share | (Numerator) | (Denominator) | Share |
| | | | Amount | | | Amount |
| Basic EPS | | | | | | |
| Net income from continuing operations | \$ 23,578 | | \$ 0.62 | \$ 11,151 | | \$ 0.32 |
| Discontinued operations | | | | | | |
| Income allocable to common shares | \$ 23,578 | 37,919,842 | \$ 0.62 | \$ 11,151 | 34,800,580 | \$ 0.32 |
| Effect of Dilutive Securities | | | | | | |
| Options and deferred shares | | 512,745 | | | 340,388 | |
| Diluted EPS | | | | | | |
| Net income from continuing operations | \$ 23,578 | | \$ 0.61 | \$ 11,151 | | \$ 0.32 |
| Discontinued operations | | | | | | |
| Income allocable to common shares plus assumed conversions | \$ 23,578 | 38,432,587 | \$ 0.61 | \$ 11,151 | 35,140,968 | \$ 0.32 |
| | | | | | | |
| | For the six months ended June 30, 2005 | | | For the six months ended June 30, 2004 | | |
| | Income | Shares | Per | Income | Shares | Per |
| | (Numerator) | (Denominator) | Share | (Numerator) | (Denominator) | Share |
| | | | Amount | | | Amount |
| Basic EPS | | | | | | |
| Net income from continuing operations | \$ 25,809 | | \$ 0.69 | \$ 9,355 | | \$ 0.27 |
| Discontinued operations | | | | | | |
| Cumulative effect of a change in accounting principle | | | | 520 | | 0.02 |
| Income allocable to common shares | \$ 25,809 | 37,404,006 | \$ 0.69 | \$ 9,875 | 34,047,243 | \$ 0.29 |
| Effect of Dilutive Securities | | | | | | |
| Options and deferred shares | | 486,905 | | | 359,120 | |

Diluted EPS

| | | | | | | |
|--|-----------|------------|---------|----------|------------|---------|
| Net income from continuing operations | \$ 25,809 | | \$ 0.68 | \$ 9,355 | | \$ 0.27 |
| Discontinued operations | | | | | | |
| Cumulative effect of a change in accounting principle | | | | 520 | | 0.02 |
| Income allocable to common shares plus assumed conversions | \$ 25,809 | 37,890,911 | \$ 0.68 | \$ 9,875 | 34,406,363 | \$ 0.29 |

NOTE 14 RELATED PARTY TRANSACTIONS AND TRANSACTIONS WITH AFFILIATES AND NON-PROFIT ENTITIES

From time to time, borrowers have defaulted on their debt obligations to the Company. Some of these obligations were incurred in connection with the development of properties that collateralize the Company's tax-exempt bonds. These properties are sometimes referred to as defaulted assets. In a number of these circumstances, the Company has, after evaluating its options, chosen not to foreclose on the property. Instead, the Company has negotiated the transfer of a property's deed in lieu of foreclosure to, or replaced the general partner of an original borrowing partnership with, an entity controlled by certain officers of the Company, including MMA Affordable Housing, Inc. (**MMAH**) and MuniMae Foundation, Inc. (**MMF**). The Company has taken this action to preserve the value of the original tax-exempt bond obligations and to maximize cash flow from the defaulted assets. The officers receive no monetary benefit from these transactions. Following the transfer of a property to, or replacement of the general partner with, such entity, that entity controls the defaulted or previously defaulted asset, which serves as collateral for the debt to the Company.

During 2005, certain developers opted or were required to transfer to the Company or an affiliate of the Company all of their rights and interests in eleven properties, as the developers had encountered substantial financial difficulties and/or had inadequately managed and supervised development of the underlying properties. Seven of the eleven properties were financed, in whole or in part, through equity investments from tax credit equity funds that the Company sponsored (including some from guaranteed funds) and tax-exempt bond or taxable loan investments held by the Company. Three of the eleven properties had no Company debt and were financed in part by equity investments from tax credit equity funds that the Company sponsored. One of the eleven properties had no equity investment sponsored by the Company and was financed in part by a tax-exempt bond investment and a taxable loan investment held by the Company. The general partner interests in ten of the property partnerships were transferred to MMAH. The sole member interest in one of the property partnerships that is a not-for-profit was transferred to MMF. The total carrying value of the Company's investments in these properties was \$61.8 million as of June 30, 2005. The Company is continuing to evaluate the possibility of impairment related to all of the above-mentioned investments as each relates to the Company. At this time, the facts and circumstances surrounding each investment and the possible outcomes are uncertain. No other-than-temporary impairment is currently probable or estimable as no single outcome has a high probability of occurring. As of June 30, 2005, no other-than-temporary impairment has been recorded in the accompanying condensed consolidated income statement for these investments. However, certain of the tax-exempt bonds have been recorded at a fair value below amortized cost through a charge to other comprehensive income.

The Company is exposed to the following risks associated with the above-mentioned investments: (1) we could be required to provide loans to the partnerships in order to complete the construction or rehabilitation of certain properties and to achieve stabilization of those properties which are not substantially leased; (2) the tax-exempt bonds secured by properties held in these partnerships could become other-than-temporarily impaired resulting in a loss recorded in the income statement; (3) we could be called upon to make payments pursuant to our yield guarantees related to properties held in sponsored guaranteed funds; (4) a bankruptcy by or against the replaced general partners or the construction companies involved in these properties or its affiliates may give rise to additional claims concerning these partnerships; and (5) we may foreclose on the properties related to our debt investments, which foreclosure could result in losses to the Company.

NOTE 15 BUSINESS SEGMENT REPORTING

The Company has three reportable business segments: (1) an investing segment consisting primarily of subsidiaries producing tax-exempt interest income through investments in tax-exempt bonds, interests in bond securitizations, taxable loans and derivative financial instruments; (2) a tax credit equity segment consisting of subsidiaries that primarily generate fees by providing tax credit equity syndication and asset management services; and (3) a real estate finance segment consisting of subsidiaries that primarily generate taxable fee income by providing loan servicing, loan origination, advisory and other related services. The real estate finance segment includes certain new business/product initiatives of the Company and encompasses our fiduciary responsibilities to our institutional investor clients. Segment results include all direct revenues and expenses of each segment and allocations of indirect

expenses based on specific methodologies. The Company's reportable segments are strategic business units that primarily generate different income streams and are managed separately. The following tables reflect the results of the Company's business segments for the three and six months ended June 30, 2005 and 2004.

Municipal Mortgage & Equity, LLC
SEGMENT REPORTING FOR THE THREE MONTHS ENDED JUNE 30, 2005 AND 2004
(in thousands)

| | | | 2005 | | |
|---|-------------|------------------------|-------------|----------------|-----------------------|
| | Investing | Real Estate Finance | Tax Credit | Adjustments | Total Consolidated |
| INCOME STATEMENT DATA | | | | | |
| Total interest income | \$ 28,900 | \$ 10,721 | \$ 1,544 | \$ (4,145)(1) | \$ 37,020 |
| Total fee income | 224 | 6,833 | 12,181 | (1,283)(2) | 17,955 |
| Net rental income | | | 5,550 | | 5,550 |
| Total operating income | 29,124 | 17,554 | 19,275 | (5,428) | 60,525 |
| Net income (loss) | 32,392 | (4,627) | (2,904) | (1,283) | 23,578 |
| Depreciation and amortization | 36 | 892 | 3,009 | | 3,937 |
| Net income (loss) from equity investments in partnerships | 15,526 | 527 | (25,383) | | (9,330) |
| BALANCE SHEET DATA | | | | | |
| Total assets | \$1,761,950 | \$903,949 | \$939,157 | \$(265,309)(3) | \$3,339,747 |
| | | | 2004 | | |
| | Investing | Real Estate Finance | Tax Credit | Adjustments | Total Consolidated |
| INCOME STATEMENT DATA | | | | | |
| Total interest income | \$ 27,309 | \$ 9,743 | \$ 2,565 | \$ (5,030)(1) | \$ 34,587 |
| Total fee income | 294 | 6,236 | 7,677 | (1,344)(2) | 12,863 |
| Net rental income | | | 5,496 | | 5,496 |
| Total operating income | 27,603 | 15,979 | 15,738 | (6,374) | 52,946 |
| Net income (loss) | 21,284 | (403) | (8,386) | (1,344) | 11,151 |
| Depreciation and amortization | 44 | 587 | 3,305 | | 3,936 |
| Net income (loss) from equity investments in partnerships | 521 | | (71,745) | | (71,224) |
| BALANCE SHEET DATA | | | | | |
| Total assets | \$1,593,506 | \$709,714 | \$2,011,485 | \$(230,674)(3) | \$4,084,031 |

(1) Adjustments represent intercompany interest and expense that are eliminated in consolidation.

- (2) Adjustments represent origination fees on purchased investments, which are deferred and amortized into income over the life of the investment
- (3) Adjustment represents intercompany receivables and payables that are eliminated in consolidation.

Municipal Mortgage & Equity, LLC
SEGMENT REPORTING FOR THE SIX MONTHS ENDED JUNE 30, 2005 AND 2004
(in thousands)

| | | | 2005 | | |
|---|-------------|------------------------|-------------|----------------|-----------------------|
| | Investing | Real Estate Finance | Tax Credit | Adjustments | Total Consolidated |
| INCOME STATEMENT DATA | | | | | |
| Total interest income | \$ 56,708 | \$ 21,591 | \$ 2,127 | \$ (7,888)(1) | \$ 72,538 |
| Total fee income | 411 | 11,486 | 25,264 | (2,943)(2) | 34,218 |
| Net rental income | | | 12,122 | | 12,122 |
| Total operating income | 57,119 | 33,077 | 39,513 | (10,831) | 118,878 |
| Net income (loss) | 49,751 | (9,990) | (11,009) | (2,943) | 25,809 |
| Depreciation and amortization | 68 | 1,371 | 6,292 | | 7,731 |
| Net income (loss) from equity investments in partnerships | 16,290 | 911 | (71,257) | | (54,056) |
| BALANCE SHEET DATA | | | | | |
| Total assets | \$1,761,950 | \$903,949 | \$939,157 | \$(265,309)(3) | \$3,339,747 |
| | | | 2004 | | |
| | Investing | Real Estate Finance | Tax Credit | Adjustments | Total Consolidated |
| INCOME STATEMENT DATA | | | | | |
| Total interest income | \$ 53,847 | \$ 19,468 | \$ 3,393 | \$ (11,091)(1) | \$ 65,617 |
| Total fee income | 564 | 10,156 | 19,691 | (2,397)(2) | 28,014 |
| Net rental income | | | 5,496 | | 5,496 |
| Total operating income | 54,411 | 29,624 | 28,580 | (13,488) | 99,127 |
| Net income (loss) | 32,096 | (3,881) | (15,944) | (2,396) | 9,875 |
| Depreciation and amortization | 86 | 1,106 | 4,683 | | 5,875 |
| Net income (loss) from equity investments in partnerships | 160 | | (81,895) | | (81,735) |
| BALANCE SHEET DATA | | | | | |
| Total assets | \$1,593,506 | \$709,714 | \$2,011,485 | \$(230,674)(3) | \$4,084,031 |

(1) Adjustments represent intercompany interest and expense that are eliminated in consolidation.

(2) Adjustments represent origination fees on purchased investments, which are deferred and amortized into income over the life of the investment

(3) Adjustment represents intercompany receivables and payables that are eliminated in consolidation.

NOTE 16 DISCONTINUED OPERATIONS

In January and March of 2005, certain Project Partnerships property was sold for net proceeds of \$1.8 million. Approximately \$6.9 million of the Project Partnerships liabilities were forgiven and included in the overall gain to the partnerships. The Company holds a less than 1% general partner interest in the Project Partnerships and therefore, the activities related to these properties, including the associated gain on disposal, are de minimis to the Company. The Company as general partner received no proceeds from the sale. The net assets of the properties as of the date of sale were approximately as follows:

(in thousands)

| | |
|---------------------------------------|-----------|
| Fixed assets | \$ 15,397 |
| Other assets | 274 |
| Other liabilities | (12,248) |
| Net assets of discontinued operations | \$ 3,423 |

NOTE 17 SUBSEQUENT EVENTS

On July 1, 2005, the Company completed the acquisition of Glaser Financial Group, Inc. (**Glaser**). Glaser is a full service commercial mortgage banker that arranges financing predominately in the upper Midwest for multifamily, senior housing and commercial real estate through Fannie Mae DUS, Freddie Mac, HUD/FHA, conventional and conduit funding sources. The purchase price included a combination of cash and stock totaling approximately \$67.0 million, assuming certain performance metrics are achieved. Glaser's current servicing portfolio totals approximately \$3.5 billion and is comprised of approximately 64,000 units including both insured and uninsured taxable loans and tax-exempt bond issues. The initial payment of \$50.0 million was financed primarily through the sale of approximately \$38.8 million in Trust Preferred Securities (see Note 10). The remainder of the initial portion of the purchase price is being funded through cash on hand.

In connection with the acquisition, the Company entered into an Amended and Restated Credit Agreement (**Credit Agreement**) effective as of July 1, 2005 with U.S. Bank National Association (**U.S. Bank**). The Credit Agreement provides for revolving loans to the Company to finance specified types of mortgage loans, investments and advances in an amount of up to \$255.0 million, subject to sub-limits for particular classifications of borrowings. The revolving loans have varying maturities of up to 90 days as agreed upon between the Company and U.S. Bank, and all revolving loans mature not later than September 30, 2005. Depending on the type of borrowing, revolving loans bear interest at either U.S. Bank's prime rate or a floating rate, reset daily, equal to the one-month LIBOR rate plus a spread. The revolving loans are secured by a first priority lien on specified loans, mortgages, investments and advances financed under the Credit Agreement.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**General Business**

The Company provides debt and equity financing to developers of multifamily housing and other types of commercial real estate. 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. Interest income derived from the majority of these 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 and other types of real estate, and servicing, underwriting, structuring and managing of commercial real estate investments, both for the Company's own account and on behalf of third parties. These investments generate income that is includable income 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 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. The Company posts all reports filed with the SEC on its website at <http://www.munimae.com>. The Company also makes available free of charge its Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those Reports filed pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after the Company electronically files such material with the SEC. These reports are also available free of charge by contacting Angela Richardson in Investor Relations at 621 E. Pratt Street, Suite 300, Baltimore, Maryland, 21202 or info@munimae.com or by calling 888-788-3863.

Overview

Net income increased \$12.4 million and \$15.9 million for the three and six months ended June 30, 2005, respectively, over the same periods in 2004. The increases are primarily driven by increases of \$5.1 million and \$6.2 million in fee

income and \$4.9 million and \$9.4 million in net gain on sales offset by increases in operating expenses of \$1.0 million and \$9.0 million for the three and six months ended June 30, 2005, respectively, over the same periods in 2004. In addition, the Company recorded \$0.6 million and \$1.4 million in impairments and valuation allowances related to certain bonds, taxable loans and equity method investments for the three and six months ended June 30, 2005, respectively.

In February 2005, the Company completed the acquisition of MONY Realty Capital, Inc. (**MRC**) from AXA Financial, Inc. for a total purchase price of \$10.9 million. **MRC** sources, underwrites, structures, closes and manages commercial real estate investments and is included in the Company's real estate finance segment. Part of the purchase agreement requires that

the Company commit to invest \$25.0 million in a real estate partnership in which MRC is already a general partner. As of June 30, 2005, the Company had funded \$7.9 million of its commitment.

On July 1, 2005, the Company completed the acquisition of Glaser Financial Group, Inc. (**Glaser**). Glaser is a full service commercial mortgage banker that arranges financing predominately in the upper Midwest for multifamily, senior housing and commercial real estate through Fannie Mae DUST™, Freddie Mac, HUD/FHA, conventional and conduit funding sources. The purchase price included a combination of cash and common shares totaling approximately \$67.0 million, assuming certain performance metrics are achieved. The initial payment of \$50.0 million was financed primarily through the sale of approximately \$38.8 million in Trust Preferred Securities. The remainder of the initial portion of the purchase price is being funded through cash on hand. In connection with the acquisition, the Company entered into an Amended and Restated Credit Agreement (**Credit Agreement**) effective as of July 1, 2005 with U.S. Bank National Association. The Credit Agreement provides for revolving loans to the Company to finance specified types of mortgage loans, investments and advances in an amount of up to \$255.0 million, subject to sub-limits for particular classifications of borrowings.

Liquidity and Capital Resources

Capital

The Company relies on the regular availability of capital from equity and debt offerings, securitization transactions, bank lines of credit, pension funds and government sponsored enterprises (**GSEs**) to finance its growth. The Company's sources of capital are discussed below.

The Company expects to meet its cash needs in the short-term, which consist primarily of funding of new investments, payment of distributions to shareholders, funding the warehousing of operating partnerships for syndication activities and funding of real estate finance activities, from securitization transactions, equity and debt offering proceeds, warehousing facilities and lines of credit with banks, finance companies and pension funds and cash on hand. To continue to grow these activities, the Company will need to increase its access to capital during the remainder of 2005 and in future years. The Company expects it will need approximately \$300 million to \$500 million in new net capital during the remainder of 2005 to meet its 2005 production targets for its lending and tax credit equity businesses. The new net capital includes additional borrowings on existing lines of credit. The Company expects to continue to generate capital through the issuance of privately placed preferred and trust preferred securities and listed common shares. The Company has entered into discussions with its existing capital providers to increase their financing commitments. In addition, the Company is seeking to establish relationships with additional pension funds, investors in funds we manage, and to expand its relationships with GSEs.

In February 2005, the Company sold to the public approximately 2.6 million common shares at a price of \$26.51 per share. Net proceeds on the 2.6 million shares approximated \$64.9 million. The net proceeds from this offering were used for general corporate purposes, including funding of new investments, paying down debt and working capital.

A consolidated indirect wholly owned subsidiary of the Company, MMA Financial Holdings, Inc. (**MFH**), formed MFH Capital Trust II (**MFH Trust II**) and MFH Capital Trust III (**MFH Trust III**) in 2005 as special purpose financing entities. MFH Trust II and MFH Trust III are unconsolidated entities. On March 15, 2005, MFH Trust II sold to qualified institutional investors \$50.0 million in 8.05% Trust Preferred Securities. On June 28, 2005, MFH Trust III sold to qualified institutional investors \$38.8 million in 7.62% Trust Preferred Securities. MFH Trust II and MFH Trust III used the proceeds from the offerings to purchase Junior Subordinated Debentures issued by MFH. MFH used the March 15, 2005, offering net proceeds from the Debentures to repay a portion of a loan from an affiliate and other indebtedness of MFH and its affiliates, and for general corporate purposes. MFH loaned the June 28, 2005, net proceeds from the Debentures to an affiliate, which in turn used the proceeds towards the acquisition of Glaser.

During the first quarter of 2005, the Company purchased 56,300 of its common shares at an aggregate cost of \$1.3 million under a share repurchase program previously approved by the Board of Directors. No common shares were purchased during the second quarter of 2005.

Production

The following table summarizes the transactions structured by the Company for the three months ended June 30, 2005:

| | Second Quarter Volume |
|---|-----------------------------|
| (in millions) | |
| Taxable Construction/Permanent Lending. | \$281.3 |
| Tax-exempt Bonds Construction/Permanent | 62.5 |
| Supplemental Loans | 12.5 |
| Equity Investments | 220.2 |
| Total | \$576.5 |

The Company also raised \$215.3 million for investment in syndicated tax credit equity funds during the three months ended June 30, 2005.

Covenant Compliance

As of June 30, 2005, the Company was in compliance with all covenants applicable to its credit facilities.

Contractual Obligations

The Company's 2004 Form 10-K contains a detailed description of the Company's contractual obligations. Except as described below, there has been no material change since December 31, 2004 to the information related to the Company's contractual obligations.

In March 2005, the Company entered into a contractual arrangement whereby the counterparty to the arrangement will purchase tax-exempt bonds from the Company or a third party and hold the bonds for a minimum of 30 days. The Company will have the option to bid for the purchase of the bonds at the time of sale by the counterparty. Regardless of whether the bonds are purchased by the Company or not, the Company will pay to the counterparty or receive from the counterparty amounts for any declines or increases in the bonds' market value from the date of purchase to the date of swap termination. The arrangement is considered a derivative. The total maximum notional amount of the swap is \$50.0 million, based on the underlying value of the bonds held by the counterparty. The Company will receive a 1.50% annual fee on the outstanding notional amount of the swap. During the term of the swap, the Company is required to post collateral equal to the amount by which the purchase price of the bond or bonds subject to the swap exceeds the quoted market value by more than \$1.0 million. The arrangement has a maturity date of December 31, 2005. As of June 30, 2005, the Company had three swaps outstanding under this arrangement with a total notional amount of \$15.7 million.

During the second quarter of 2005, the Company entered into a new term financing facility of up to \$22.0 million. The facility is secured by certain taxable bonds and has a maturity date of May 1, 2010. Interest accrues at LIBOR plus a spread. In connection with this facility, the Company entered into a new interest rate swap contract with a total notional amount of \$18.4 million and an effective date in July 2005. The total notional amount of this contract is expected to increase to \$22.0 million in the third quarter of 2005. In addition to the above-mentioned interest rate swaps, the Company entered into two other interest rate swaps with a total notional amount of \$16.9 million in February of 2005.

Distribution Policy

The Company has historically sought to maximize shareholder value through increases in cash distributions to shareholders. The Company's Board of Directors declares quarterly distributions based on management's recommendation, which itself is based on evaluation of a number of factors, including the Company's retained earnings, business prospects and available cash.

The Company's distributions per common share for the six months ended June 30, 2005 and 2004 totaled \$0.9600 and \$0.9200, respectively.

Cash Flow

At June 30, 2005 and 2004, the Company had cash and cash equivalents of approximately \$136.7 million and \$100.0 million, respectively. Cash flow from operating activities was \$0.3 million and \$23.5 million for the six months ended June 30, 2005 and 2004, respectively. The \$23.2 million decrease in operating cash flow for 2005 versus 2004 is due primarily to a decrease in net changes in assets and liabilities of \$24.4 million, a net decrease in non-cash items, tax benefits and income allocable to preferred shareholders of \$8.0 million, an increase in net gain on sales of \$7.2 million, offset by an increase in net income before cumulative effect of a change in accounting principle of \$16.4 million.

Off-Balance-Sheet Arrangements

The Company may invest in bonds that are subordinate in priority of payment to senior bonds that are owned by a third party. Such senior bonds represent off-balance-sheet debt for the Company. These senior bonds that are not reflected on the Company's balance sheet at June 30, 2005 and December 31, 2004 totaled \$11.7 million and \$11.9 million, respectively (face amount).

The Company securitizes bonds and other assets in order to enhance its overall return on its investments and to generate proceeds that facilitate the acquisition of additional investments. The Company uses various programs to

facilitate the securitization and credit enhancement of its bond investments. For a description of a typical bond securitization structure, see further discussion under *Liquidity and Capital Resources* in the Company's 2004 Form 10-K. The substantial majority of the Company's securitizations are reflected as indebtedness on its consolidated balance sheet, and off-balance-sheet securitizations are not material to the Company's liquidity and capital needs. At June 30, 2005 and December 31, 2004, the Company's total off-balance-sheet debt relating to securitizations totaled \$73.9 million and \$144.1 million, respectively.

Guarantees

The Company's maximum exposure under its guarantee obligations may not be indicative of the likelihood of the expected loss under the guarantees. The following table summarizes the Company's guarantees by type at June 30, 2005.

| (in millions) | | June 30, 2005 | | |
|---|------|------------------|-----------------|--|
| Guarantee | Note | Maximum Exposure | Carrying Amount | Supporting Collateral |
| Loss-sharing agreements with Fannie Mae, GNMA and HUD | (1) | \$ 195.3 | \$ | \$4.0 million letter of credit pledged |
| Bank line of credit guarantees | (2) | 173.2 | 173.2 | \$200.2 million of investment in partnership, loans receivable, tax-exempt and taxable bonds |
| Tax credit-related guarantees | (3) | 513.8 | 232.3 | \$48.3 million of cash, tax-exempt bonds, loans receivable and letters of credit |
| Other financial/payment guarantees | (4) | 471.0 | 312.4 | \$542.9 million of cash, equity and tax-exempt bonds |
| Put options | (5) | 69.6 | | \$60.3 million of tax-exempt bonds |
| Letter of credit guarantees | (6) | 131.4 | 65.0 | \$11.6 million of cash and loans receivable |
| Indemnification contracts | (7) | 77.2 | 26.1 | None |
| Trust preferred guarantees | (8) | 174.1 | 174.1 | None |
| | | \$1,805.6 | \$983.1 | |

(1) As a Fannie Mae DUS lender and GNMA loan servicer, the Company may share in losses relating to underperforming real estate mortgage loans delivered to Fannie Mae and GNMA. More specifically, if the borrower fails to make a payment of principal, interest, taxes or insurance premiums on a DUS loan

originated by the Company and sold to Fannie Mae, the Company may be required to make servicing advances to Fannie Mae.

Also, the Company may participate in a deficiency after foreclosure on Fannie Mae DUS and GNMA loans. The term of the loss sharing agreement is based on the contractual requirements of the underlying loans delivered to Fannie Mae and GNMA, which varies to a maximum of 40 years.

- (2) The Company provides payment or performance guarantees for certain borrowings under line of credit facilities. The amount outstanding under these lines of credit was \$172.0 million at June 30, 2005. This amount is included in notes payable in the Company's consolidated

balance sheet.

(3) The Company acquires and sells interests in partnerships that provide low-income housing tax credits for investors. In conjunction with the sale of these partnership interests, the Company may provide performance guarantees on the underlying properties owned by the partnerships or guarantees to the fund investors. These guarantees have various expirations to a maximum term of 20 years.

(4) The Company has entered into arrangements that require the Company to make payments in the event a specified third party fails to perform on its financial obligation. The Company typically provides these guarantees in conjunction with the sale of an asset to a third party or the

Company's investment in equity ventures. The term of the guarantee varies based on loan payoff schedules or Company divestitures.

- (5) The Company has entered into put option agreements with counterparties whereby the counterparty has the right to sell to the Company, and the Company has the obligation to buy, an underlying investment at a specified price. These put option agreements expire at various dates through June 2010.
- (6) The Company provides a guarantee of the repayment on losses incurred under letters of credit issued by third parties or to provide substitute letters of credit at a predetermined future date. In addition, the Company may provide a payment guarantee for certain assets in securitization

programs. These guarantees expire at various dates through September 2007.

- (7) The Company has entered into indemnification contracts, which require the guarantor to make payments to the guaranteed party based on changes in an underlying investment that is related to an asset or liability of the guaranteed party. These agreements typically require the Company to reimburse the guaranteed party for legal and other costs in the event of an adverse judgment in a lawsuit or the imposition of additional taxes due to a change in the tax law or an adverse interpretation of the tax law. The term of the indemnification varies based on the underlying program life, loan payoffs, or Company divestitures. Based on the terms of the underlying contracts, the

maximum exposure amount only includes amounts that can be reasonably estimated at this time. The actual exposure amount could vary significantly.

- (8) The Company provides a payment guarantee of the underlying trust preferred securities issued. The guarantee obligation is unsecured and subordinated to the Company's existing and future debt and liabilities except for debt and liabilities which by their terms are specifically subordinated to the guarantee obligations and the rights of the holders of various classes of existing and future preferred shares of the Company.

Results of Operations and Critical Accounting Estimates

Critical Accounting Policies and Estimates

The Company's 2004 Form 10-K contains a detailed description of the Company's critical accounting policies and estimates. There has been no material change to the information related to critical accounting policies and estimates since December 31, 2004, except as noted under the "New Accounting Pronouncements" section in Note 1 to the Condensed Consolidated Financial Statements included in this Report.

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 for public companies that 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.

In June 2005, the FASB ratified the consensus in EITF Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights" (**Issue 04-5**), which provides guidance in determining whether a general partner controls a limited partnership. To promote consistency in applying this guidance to corporate entities and those entities that hold real estate:

the EITF amended Issue No. 96-16, "Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Interest Shareholder or Shareholders Have Certain Approval or Veto Rights" (Issue 96-16), and

the FASB staff issued FSP No. SOP 78-9-1, which amends AICPA Statement of Position 78-9, "Accounting for Investments in Real Estate Ventures," to reflect the consensus reached in Issue 04-5.

The effective date for applying the guidance in Issue 04-5 and FSP SOP 78-9-1 is (1) June 29, 2005, for all new limited partnerships and existing limited partnerships for which the partnership agreements are modified and (2) no later than the beginning of the first reporting period in fiscal years beginning after December 15, 2005, for all other limited partnerships. Thus far, the impact of Issue 04-5 has had no effect on the Company's financial statements. The Company will continue to evaluate the impact of Issue 04-5 throughout the remainder of 2005.

Results of Operations**Net Interest Income**

| | For the three months ended June 30, | | | | For the six months ended June 30, | | | |
|---|-------------------------------------|---------------|------------------|---------------|-----------------------------------|---------------|------------------|---------------|
| | 2005 | % | 2004 | % | 2005 | % | 2004 | % |
| (in thousands) | | | | | | | | |
| Interest on bonds and interests in bond securitizations | \$ 24,361 | 199.1% | \$ 21,340 | 178.9% | \$ 47,446 | 186.8% | \$ 40,842 | 156.9% |
| Interest on loans | 11,665 | 95.3 | 11,388 | 95.4 | 23,611 | 92.9 | 22,109 | 85.0 |
| Interest on short-term investments | 994 | 8.1 | 1,859 | 15.6 | 1,481 | 5.8 | 2,666 | 10.2 |
| Total interest income | 37,020 | | 34,587 | | 72,538 | | 65,617 | |
| Interest expense | (18,702) | (152.8) | (18,651) | (156.3) | (35,819) | (141.0) | (32,544) | (125.0) |
| Interest expense on debentures and preferred shares | (6,081) | (49.7) | (4,004) | (33.6) | (11,312) | (44.5) | (7,049) | (27.1) |
| Net interest income | \$ 12,237 | 100.0% | \$ 11,932 | 100.0% | \$ 25,407 | 100.0% | \$ 26,024 | 100.0% |

In the table above, interest on short-term investments and interest expense include the effects of the financing method and consolidation of the tax credit equity funds. Net interest income increased \$0.3 million for the three months ended June 30, 2005, as compared to the same period in 2004, primarily due to: (1) a \$3.0 million net increase in interest on bonds and interests in bond securitizations resulting from (i) new investments in tax-exempt bonds producing \$5.8 million of interest income, (ii) increased funding of existing investments in tax-exempt bonds producing \$2.7 million of interest income, (iii) \$0.5 million of interest income from new investments in taxable bonds, offset by (iv) an increase in defaulted and non-accrual bonds that decreased interest income \$2.6 million and (v) a reduction of \$4.0 million in interest income due to sales and restructuring of underlying tax-exempt bond investments coupled with other net increases in bond interest income of \$0.6 million; (2) a \$0.3 million increase in interest on loans due to an increase in the average loan receivable balance; (3) a \$0.9 million decrease in interest on short-term investments due primarily to (i) a decrease of \$2.1 million in interest on short-term investments related to fluctuations in short-term investment accounts and interest charged to tax credit equity funds on warehoused properties offset by (ii) an increase of \$1.2 million in interest on short-term investments related to the financing method and consolidation of tax credit equity funds; (4) a slight increase in interest expense resulting from (i) an increase of \$0.5 million from senior costs in new securitizations combined with increases in underlying borrowing rates offset by (ii) a \$0.5 million decrease in interest expense related to the financing method and consolidation of tax credit equity funds; and (5) a \$2.1 million increase in interest expense on debentures and preferred shares resulting from the interest expense and related amortization of debt issue costs applicable to the issuance of the \$172.8 million of trust preferred securities issued in May and September of 2004 and March and June of 2005. The above-mentioned fluctuations related to the financing method and consolidation of tax credit partnerships are primarily related to the elimination of intercompany interest from the consolidated tax credit equity funds and the financing method as well as the interest expense related to the consolidated Project Partnerships.

During the three months ended June 30, 2005 and 2004, \$0.9 million and \$0 million, respectively, of interest expense on preferred shares was recorded as net income allocable to minority interest. These preferred shares are recorded as preferred shareholders equity in a subsidiary company and were issued in October of 2004. Including these amounts as interest expense above results in an overall decrease of \$0.6 million in net interest income.

Net interest income decreased \$0.6 million for the six months ended June 30, 2005, as compared to the same period in 2004, primarily due to: (1) a \$6.6 million net increase in interest on bonds and interests in bond securitizations resulting from (i) new investments in tax-exempt bonds producing \$9.6 million of interest income, (ii) increased funding of existing investments in tax-exempt bonds producing \$4.7 million of interest income, (iii) \$0.5 million of interest income from new investments in taxable bonds, offset by (iv) an increase in defaulted and non-accrual bonds

that decreased interest income \$5.1 million and (v) a reduction of \$4.3 million in interest income due to sales and restructuring of underlying tax-exempt bond investments coupled with other net increases in bond interest income of \$1.2 million; (2) a \$1.5 million increase in interest on loans due to an increase in the average loan receivable balance; (3) a \$1.2 million decrease in interest on short-term investments due primarily to (i) a decrease of \$2.0 million in interest on short-term investments related to fluctuations in short-term investment accounts and interest charged to tax credit equity funds on warehoused properties offset by (ii) an increase of \$0.8 million in interest on short-term investments related to the financing method and consolidation of tax credit equity funds; (4) an increase of \$3.2 million in interest expense resulting from (i) an increase of \$1.1 million from senior costs in new securitizations combined with increases in underlying borrowing rates and an increase of (ii) \$2.1 million in

interest expense related to the financing method and consolidation of tax credit equity funds; and (5) a \$4.3 million increase in interest expense on debentures and preferred shares resulting from the interest expense and related amortization of debt issue costs applicable to the issuance of the \$172.8 million of trust preferred securities issued in May and September of 2004 and March and June of 2005. The above-mentioned fluctuations related to the financing method and consolidation of tax credit partnerships are primarily related to the elimination of intercompany interest from the consolidated tax credit equity funds and the financing method as well as the interest expense related to the consolidated Project Partnerships.

During the six months ended June 30, 2005 and 2004, \$1.9 million and \$0 million, respectively, of interest expense on preferred shares was recorded as net income allocable to minority interest. These preferred shares are recorded as preferred shareholders equity in a subsidiary company and were issued in October of 2004. Including these amounts as interest expense above results in an overall decrease of \$2.5 million in net interest income.

Fee Income

| | For the three months ended June 30, | | | | For the six months ended June 30, | | | |
|------------------------------------|-------------------------------------|---------------|-----------------|---------------|-----------------------------------|---------------|-----------------|---------------|
| | 2005 | % | 2004 | % | 2005 | % | 2004 | % |
| (in thousands) | | | | | | | | |
| Syndication fees | \$ 4,424 | 24.6% | \$ 4,190 | 32.6% | \$ 9,032 | 26.4% | \$ 7,941 | 28.4% |
| Origination and brokerage fees | 1,410 | 7.9 | 2,848 | 22.1 | 1,845 | 5.4 | 3,765 | 13.4 |
| Guarantee fees | 4,039 | 22.5 | 1,506 | 11.7 | 6,975 | 20.4 | 3,359 | 12.0 |
| Asset management and advisory fees | 5,344 | 29.8 | 1,967 | 15.3 | 11,030 | 32.2 | 8,133 | 29.0 |
| Loan servicing fees | 1,350 | 7.5 | 1,139 | 8.9 | 2,572 | 7.5 | 2,258 | 8.1 |
| Other income | 1,388 | 7.7 | 1,213 | 9.4 | 2,764 | 8.1 | 2,558 | 9.1 |
| Total fee income | \$17,955 | 100.0% | \$12,863 | 100.0% | \$34,218 | 100.0% | \$28,014 | 100.0% |

The table above includes the effects of the financing method and the consolidation of tax credit equity funds.

Syndication fees, asset management and advisory fees, guarantee fees and other income are all affected by either or both of the financing method and the consolidation of tax credit equity funds. For the three months ended June 30, 2005, total fee income increased \$5.1 million over the same period for 2004. The effects of the financing method and the consolidation of tax credit equity funds account for \$8.7 million of the overall increase. These effects are primarily the result of eliminating syndication fees, asset management fees and other income earned by the Company from the consolidated tax credit equity funds and guarantee fee income generated from the finance method. This increase of \$8.7 million together with the following fluctuations which net to a decrease of \$3.6 million result in the overall increase of \$5.1 million in total fee income: (1) a decrease of \$2.6 million in syndication fees due to a decrease in overall volume; (2) a decrease of \$1.4 million in origination and brokerage fees due to (i) a decrease of \$2.5 million in fees driven by a change in origination structure of taxable loans offset by (ii) an increase of \$1.1 million from our MRC business; (3) an increase of \$1.0 million in guarantee fees primarily due to an increase in the number of guaranteed funds; (4) a decrease of \$0.7 million in asset management and advisory fees resulting primarily from an increase in projected reserve levels and a decrease in other advisory fees; (5) an increase of \$0.2 million in loan servicing fees due to an increase in our servicing portfolio including fees from our MRC business; and (6) a decrease of \$0.1 million in other income.

For the six months ended June 30, 2005, total fee income increased \$6.2 million over the same period for 2004. The effects of the financing method and the consolidation of tax credit equity funds account for \$6.5 million of the overall increase. These effects are primarily the result of eliminating syndication fees, asset management fees and other income earned by the Company from the consolidated tax credit equity funds and guarantee fee income generated from the finance method. This increase of \$6.5 million together with the following fluctuations which net to a decrease of \$0.3 million result in the overall increase of \$6.2 million in total fee income: (1) an increase of \$0.3 million in syndication fees due to an increase in overall volume; (2) a decrease of \$1.9 million in origination and brokerage fees due to (i) a decrease of \$3.1 million in fees driven by a change in origination structure of taxable loans offset by (ii) an increase of \$1.2 million from our MRC business; (3) an increase of \$1.0 million in guarantee fees

primarily due to an increase in the number of guaranteed funds; (4) a decrease of \$0.1 million in asset management and advisory fees primarily the result from an increase in projected reserve levels and a decrease in other advisory fees; (5) an increase of \$0.3 million in loan servicing fees due to an increase in our servicing portfolio including fees from our MRC business; and (6) an increase of \$0.1 million in other income.

Net Rental Income

At times, the Company takes ownership of the general partnership interest in the underlying Project Partnerships in which the tax credit equity funds are the limited partners. The Company takes a 0.01% to 1% general partner interest in the Project Partnership, and the tax credit equity fund, which the Company may also consolidate, is typically the 99.99% to 99% limited partner. Net rental income represents income from the Project Partnerships that were consolidated by the Company effective March 31, 2004. Net rental income remained relatively unchanged for the three months ended June 30, 2005. Net rental income increased \$6.6 million for the six months ended June 30, 2005 over the same period for 2004 due to three months of operations reflected in 2004 versus six months of operations in 2005.

Net Gain on Sales

| | For the three months ended June 30, | | | | For the six months ended June 30, | | | |
|---|-------------------------------------|---------------|----------------|---------------|-----------------------------------|---------------|----------------|---------------|
| | 2005 | % | 2004 | % | 2005 | % | 2004 | % |
| (in thousands) | | | | | | | | |
| Net gain on sale of loans | \$ 1,251 | 8.5% | \$1,730 | 17.6% | \$ 965 | 5.1% | \$2,410 | 24.9% |
| Net gain on sale of tax-exempt investments | 5,159 | 35.0 | 1,013 | 10.3 | 6,073 | 31.8 | 1,205 | 12.4 |
| Net gain on sale of investments in tax credit equity partnerships | 5,723 | 38.9 | 379 | 3.9 | 6,564 | 34.4 | 2,814 | 29.0 |
| Net gain on deconsolidation of tax credit equity partnerships | 2,501 | 17.0 | | | 2,501 | 13.1 | | |
| Net gain on derivatives | 94 | 0.6 | 6,687 | 68.2 | 2,982 | 15.6 | 3,262 | 33.7 |
| Total net gain on sales | \$14,728 | 100.0% | \$9,809 | 100.0% | \$19,085 | 100.0% | \$9,691 | 100.0% |

Net gain on sales increased \$4.9 million for the three months ended June 30, 2005, as compared to the same period in 2004, due primarily to: (1) a \$0.5 million decrease in net gain on sale of loans primarily resulting from a reduction in gains from mortgage servicing rights assets; (2) a \$4.2 million increase in net gain on sale of tax-exempt investments due to the repayment of nine tax-exempt bonds generating \$5.2 million of gain versus the sale or repayment of four tax-exempt bonds in 2004 generating \$1.0 million of gain; (3) a \$3.4 million increase in net gain on sale of investments in tax credit equity partnerships resulting from fluctuations in the operating results and time held of certain Project Partnerships temporarily owned by the Company prior to sale to tax credit equity funds; (4) a \$2.5 million increase in gain on deconsolidation of tax credit equity partnerships due to the deconsolidation of one tax credit equity fund in 2005 versus zero in 2004; (5) a \$6.6 million decrease in net gain on derivatives primarily driven by market fluctuations in the value of the Company's derivatives; and (6) a net increase of \$1.9 million to net gain on sales related to the financing method and consolidation of the tax credit equity funds. This increase primarily relates to the elimination of the gains recorded on sales of investments in tax credit equity partnerships to consolidated tax credit equity funds and the gains recorded on the extinguishment of guarantees under the finance method.

Net gain on sales increased \$9.4 million for the six months ended June 30, 2005, as compared to the same period in 2004, due primarily to: (1) a \$1.5 million decrease in net gain on sale of loans primarily resulting from (i) a \$1.1 million reduction in gains from mortgage servicing rights assets and (ii) a \$0.4 million decrease in gains on loans due to an overall net decrease in production volume; (2) a \$4.9 million increase in net gain on sale of tax-exempt investments due to the repayment or sale of fourteen tax-exempt bonds and one senior interest in a bond securitization generating \$6.1 million of gain versus the sale or repayment of six tax-exempt bonds in 2004 generating \$1.2 million of gain; (3) a \$0.9 million increase in net gain on sale of investments in tax credit equity partnerships resulting from fluctuations in the operating results and time held of certain Project Partnerships temporarily owned by the Company prior to sale to tax credit equity funds; (4) a \$2.5 million increase in gain on deconsolidation of tax credit equity partnerships due to the deconsolidation of one tax credit equity fund in 2005 versus zero in 2004; (5) a \$0.3 million decrease in net gain on derivatives primarily driven by market fluctuations in the value of the Company's derivatives; and (6) a net increase of \$2.9 million to net gain on sales related to the financing method and consolidation of the tax

credit equity funds. This increase primarily relates to the elimination of the gains recorded on sales of investments in tax credit equity partnerships to consolidated tax credit equity funds and the gains recorded on the extinguishment of guarantees under the financing method.

Operating Expenses

| | For the three months ended June 30, | | | | For the six months ended June 30, | | | |
|---------------------------------|-------------------------------------|---------------|------------------|---------------|-----------------------------------|---------------|------------------|---------------|
| | 2005 | % | 2004 | % | 2005 | % | 2004 | % |
| (in thousands) | | | | | | | | |
| Salaries and benefits | \$ 19,839 | 64.3% | \$ 20,460 | 68.5% | \$ 37,688 | 63.1% | \$ 36,044 | 71.2% |
| General and administrative | 7,546 | 24.5 | 6,654 | 22.3 | 16,716 | 28.0 | 10,352 | 20.5 |
| Professional fees | 3,466 | 11.2 | 2,731 | 9.2 | 5,344 | 8.9 | 4,225 | 8.3 |
| Total operating expenses | \$ 30,851 | 100.0% | \$ 29,845 | 100.0% | \$ 59,748 | 100.0% | \$ 50,621 | 100.0% |

All line items in the table above include the effects of the financing method and the consolidation of tax credit equity funds. Total operating expenses increased \$1.0 million for the three months ended June 30, 2005, over the same period for 2004 due primarily to: (1) a \$0.7 million decrease in salaries and benefits resulting from, (i) a \$2.6 million increase in salary, healthcare insurance and other compensation costs resulting from a 25% increase in headcount, offset by (ii) a \$3.3 million decrease in bonus costs due to timing differences and changes in bonus structure; (2) a \$1.6 million increase in general and administrative and professional fees due to an increase in the overall volume of Company business and increased accounting and consulting fees surrounding internal control compliance; and (3) an increase in operating expenses of \$0.1 million, after giving effect for eliminations, related to the financing method and consolidation of certain tax credit equity funds. These operating expenses are primarily attributable to the consolidated Project Partnerships.

Total operating expenses increased \$9.1 million for the six months ended June 30, 2005, over the same period for 2004 due primarily to: (1) a \$0.9 million increase in salaries and benefits resulting from, (i) a \$4.3 million increase in salary, healthcare insurance and other compensation costs resulting from a 25% increase in headcount, offset by (ii) a \$0.9 million decrease in bonus costs due to timing differences and changes in bonus structure and (iii) a decrease of \$2.5 million in compensation costs relating to our recently retired chief executive officer; (2) a \$2.5 million increase in general and administrative and professional fees due to an increase in the overall volume of Company business and increased accounting and consulting fees surrounding internal control compliance; and (3) an increase in operating expenses of \$5.7 million, after giving effect for eliminations, related to the financing method and consolidation of certain tax credit equity funds. These operating expenses are primarily attributable to the consolidated Project Partnerships.

Depreciation and Amortization

For the three months ended June 30, 2005, depreciation and amortization remained flat as compared to the same period in 2004. For the six months ended June 30, 2005, depreciation and amortization increased \$1.9 million primarily due to six months of depreciation expense from the consolidated Project Partnerships versus three months of depreciation expense for the same period in 2004.

Impairments and Valuation Allowances Related to Investments

In accordance with the Company's valuation and impairment policies, the Company recorded \$0.6 million in impairment during the second quarter of 2005 related to a warehousing investment in a real estate operating partnership. The Company recorded other-than-temporary impairments totaling \$0.4 million on one tax-exempt bond and two taxable loans with an aggregate face amount of \$10.6 million during the three months ended June 30, 2004. For the six months ended June 30, 2005, the Company recorded \$1.4 million in impairments and valuation allowances related to a warehousing investment in a real estate operating partnership as well as one bond and one taxable loan with an aggregate face amount of \$2.7 million. The Company recorded other-than-temporary impairments totaling \$0.7 million for the six months ended June 30, 2004 primarily related to three tax-exempt bonds and two taxable loans.

The Company is continuing to evaluate the possibility of impairment related to certain transfers of interests in underlying debt and equity investments to MMA Affordable Housing, Inc. (**MMAH**) and MuniMae Foundation, Inc. (**MMF**). These transfers of interests were driven by underlying developer failure relating to the construction and management of the property partnerships. At this time, the facts and circumstances surrounding each investment and

the possible outcomes are uncertain and no other-than-temporary impairment is probable or estimable. Accordingly, as of June 30, 2005, no other-than-temporary impairment has been recorded in the accompanying condensed consolidated income statement related to these investments.

Net Losses from Equity Investments in Partnerships

Net losses from equity investments in partnerships decreased \$61.9 million for the three months ended June 30, 2005, as compared to the same period in 2004, due primarily to: (1) a decrease of \$45.7 million in net losses from equity investments in partnerships resulting from the financing method and consolidation of certain tax credit equity funds driven by a decrease in the number of tax credit equity funds consolidated and (2) a \$16.2 million decrease in losses primarily attributable to (i) a

\$15.4 million increase in gains from investments in income-producing real estate operating partnerships related to the new MRC business and CAPREIT, Inc. and its affiliates (**CAPREIT**) and (ii) a \$0.8 million decrease in losses related to warehousing investments in real estate operating partnerships.

Net losses from equity investments in partnerships decreased \$27.7 million for the six months ended June 30, 2005, as compared to the same period in 2004, due primarily to: (1) a decrease of \$9.9 million in net losses from equity investments in partnerships resulting from the financing method and consolidation of certain tax credit equity funds driven by a decrease in the number of tax credit equity funds consolidated; and (2) a \$17.8 million decrease in losses primarily attributable to (i) a \$17.1 million increase in gains from investments in income-producing real estate partnerships related to the new MRC business and CAPREIT and (ii) a \$0.7 million decrease in losses related to warehousing investments in real estate operating partnerships.

Income Tax (Expense) Benefit

Income tax expense for the three months ended June 30, 2005, increased \$4.1 million as compared to the same period in 2004 due to an increase in state tax liabilities, which was partially attributable to the MRC acquisition in the first quarter of 2005 and the deferred tax liability associated with equity investments in income-producing real estate partnerships in joint ventures with CAPREIT.

The Company had income tax expense of \$3.0 million for the six months ended June 30, 2005 as compared to an income tax benefit of \$2.3 million for the same period in 2004. The \$5.3 million increase in expense is primarily attributable to an increase in the deferred tax liability associated with equity investments in income-producing real estate partnerships in joint ventures with CAPREIT.

Net Income Allocable to Minority Interest

Net income allocable to minority interest decreased \$54.6 million and \$15.9 million for the three and six months ended June 30, 2005, respectively, as compared to the same periods in 2004. The decrease in income allocable to the limited partners in consolidated tax credit equity funds is primarily attributable to a decrease in the number of tax credit equity funds consolidated during 2005 as compared to 2004. The Company typically holds a 0.01% to 1% interest in the tax credit equity funds and therefore approximately 99% of the funds' losses are shown as net income allocable to minority interest in the condensed consolidated statement of income.

Discontinued Operations

For the three and six months ended June 30, 2005 and 2004, discontinued operations reflects no activity in the condensed consolidated statement of income. During January and March of 2005, certain Project Partnerships property was sold for net proceeds of \$1.8 million. The Company holds a less than 1% general partnership interest in the Project Partnerships and therefore, the activities related to these properties, including the associated gain on disposal, are de minimis and no amount was recorded for the three and six months ended June 30, 2005.

Cumulative Effect of a Change in Accounting Principle

For the six months ended June 30, 2004, the Company recorded a cumulative effect of a change in accounting principle of \$0.5 million as a result of the adoption of FIN 46R and the consolidation of certain tax credit equity funds.

Other Comprehensive Income

For the three and six months ended June 30, 2005, the net adjustment to other comprehensive income for unrealized holding gains on tax-exempt bonds and interests in bond securitizations available for sale was \$12.9 million and \$8.8 million, respectively. After a reclassification adjustment for gains of \$5.2 million and \$6.1 million, respectively, included in net income, other comprehensive income for the three and six months ended June 30, 2005, was \$7.8 million and \$2.8 million, respectively, and total comprehensive income was \$31.3 million and \$28.6 million, respectively.

Related Party Transactions

From time to time, borrowers have defaulted on their debt obligations to the Company. Some of these obligations were incurred in connection with the development of properties that collateralize the Company's tax-exempt bonds. These properties are sometimes referred to as defaulted assets. In a number of these circumstances, the Company has, after evaluating its options, chosen not to foreclose on the property. Instead, the Company has negotiated the transfer of a property's deed in lieu of foreclosure to, or replaced the general partner of an original borrowing partnership with, an entity controlled by certain officers of the Company, including MMAH and MMF. The Company has taken this

action to preserve the value of the original tax-exempt bond obligations and to maximize cash flow from the defaulted assets. The officers receive no monetary benefit from these

transactions. Following the transfer of a property to, or replacement of the general partner with, such entity, that entity controls the defaulted or previously defaulted asset, which serves as collateral for the debt to the Company.

During 2005, certain developers opted or were required to transfer to the Company or an affiliate of the Company all of their rights and interests in eleven properties, as the developers had encountered substantial financial difficulties and/or had inadequately managed and supervised development of the underlying properties. Seven of the eleven properties were financed, in whole or in part, through equity investments from tax credit equity funds that the Company sponsored (including some from guaranteed funds) and tax-exempt bond or taxable loan investments held by the Company. Three of the eleven properties had no Company debt and were financed in part by equity investments from tax credit equity funds that the Company sponsored. One of the eleven properties had no equity investment sponsored by the Company and was financed in part by a tax-exempt bond investment and a taxable loan investment held by the Company. The general partner interests in ten of the property partnerships were transferred to MMAH. The sole member interest in one of the property partnerships that is a not-for-profit was transferred to MMF. The total carrying value of the Company's investments in these properties was \$61.8 million as of June 30, 2005. The Company is continuing to evaluate the possibility of impairment related to all of the above-mentioned investments as each relates to the Company. At this time, the facts and circumstances surrounding each investment and the possible outcomes are uncertain. No other-than-temporary impairment is currently probable or estimable as no single outcome has a high probability of occurring. As of June 30, 2005, no other-than-temporary impairment has been recorded in the accompanying condensed consolidated income statement for these investments. However, certain of the tax-exempt bonds have been recorded at a fair value below amortized cost through a charge to other comprehensive income.

The Company is exposed to the following risks associated with the above-mentioned investments: (1) we could be required to provide loans to the partnerships in order to complete the construction or rehabilitation of certain properties and to achieve stabilization of those properties which are not substantially leased; (2) the tax-exempt bonds secured by properties held in these partnerships could become other-than-temporarily impaired resulting in a loss recorded in the income statement; (3) we could be called upon to make payments pursuant to our yield guarantees related to properties held in sponsored guaranteed funds; (4) a bankruptcy by or against the replaced general partners or the construction companies involved in these properties or its affiliates may give rise to additional claims concerning these partnerships; and (5) we may foreclose on the properties related to our debt investments, which foreclosure could result in losses to the Company.

The Company's 2004 Form 10-K contains a detailed description of the Company's related party transactions. There have been no other material changes since December 31, 2004 to the information related to the Company's related party transactions.

Income Tax Considerations

The Company's 2004 Form 10-K contains a detailed description of the Company's income tax considerations. There has been no material change since December 31, 2004 to the information related to income tax considerations.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

There has been no material change since December 31, 2004 to the information included in Item 7A of the Company's 2004 Form 10-K.

Controls and Procedures

Based on their evaluation as of June 30, 2005, the Company's management, including its Chief Executive Officer and President and its Chief Financial Officer, has concluded that the Company's disclosure controls and procedures as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 are effective. No change occurred in the Company's internal control over financial reporting (as defined in Rule 13a-15(f)) during the Company's last fiscal quarter which was identified in connection with the evaluation required by Rule 13a-15(a) as materially affecting, or reasonably likely to materially affect, the Company's internal control over financial reporting.

Our on-going review and monitoring of internal control over financial reporting does not currently cover, and will not cover by the fiscal year ending December 31, 2005, MRC (formerly MONY Realty Capital, Inc.), which was acquired in February 2005 and Glaser, which was acquired in July 2005. By the end of this fiscal year, management will not be able to fully assess the effectiveness of internal control over financial reporting for these business units because MRC

and Glaser were acquired by the Company during 2005, and management believes it will not be possible for it to conduct a complete assessment of the internal controls during the integration of these entities.

However, management has commenced its assessment of MRC's internal control over financial reporting and will commence its assessment of Glaser's internal control over financial reporting during the third quarter of 2005. Management expects to have completed its assessments by December 31, 2006, the date upon which management is required to have completed its assessments of MRC and Glaser under current law. These acquisitions are described in Notes 2 and 17 to our condensed consolidated financial statements.

PART II OTHER INFORMATION**Item 2. Purchases of Equity Securities by the Issuer and Affiliated Purchasers**

The following table summarizes the Company's purchases of common shares during the first quarter of 2005:

| Period | Issuer Purchases of Equity Security | | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number of Shares that May Yet be Purchased Under the Plans or Programs (1) |
|---------------------------------------|-------------------------------------|------------------------------|--|--|
| | Total Number of Shares Purchased | Average Price Paid per Share | | |
| January 1, 2005 to January 31, 2005 | | \$ | | 1,500,000 |
| February 1, 2005 to February 28, 2005 | | | | 1,500,000 |
| March 1, 2005 to March 31, 2005 | 56,300 | 24.36 | 56,300 | 1,443,700 |
| Total | 56,300 | \$ 24.36 | 56,300 | 1,443,700 |

(1) The Company announced on July 24, 2002, a share repurchase plan authorizing a repurchase of up to 1.5 million common shares.

There were no share repurchases during the second quarter of 2005.

Item 4. Submission of Matters to a Vote of Security Holders

At the annual meeting of the Company's shareholders held on June 2, 2005, the shareholders voted on the election of certain members of the Company's board of directors. The election of the directors was passed. The shareholders elected the following directors: Charles C. Baum (34,597,090 in favor and 260,679 abstaining), Mark K. Joseph (34,617,898 in favor and 239,871 abstaining) and Arthur S. Mehlman (34,625,395 in favor and 232,374 abstaining).

Item 6. Exhibits

- 10.1 Stock Purchase Agreement, dated June 8, 2005 (filed as part of the Company's Current Report on Form 8-K filed June 8, 2005 and incorporated by reference herein).
- 10.2 Amended and Restated Credit Agreement, dated July 1, 2005, between MMA Mortgage Investment Corporation and U.S. Bank National Association (filed as part of the Company's Current Report on Form 8-K filed July 7, 2005 and incorporated by reference herein).
- 31.1 Certification of Michael L. Falcone, Chief Executive Officer, President and Director of Municipal Mortgage & Equity, LLC Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of William S. Harrison, Chief Financial Officer of Municipal Mortgage & Equity, LLC Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Michael L. Falcone, Chief Executive Officer, President and Director of Municipal Mortgage & Equity, LLC Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of William S. Harrison, Chief Financial Officer of Municipal Mortgage & Equity, LLC Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

DATE: August 4, 2005

MUNICIPAL MORTGAGE & EQUITY,
LLC

By: /s/ William S. Harrison
William Harrison
Chief Financial Officer (Duly
Authorized Officer
and Principal Financial Officer)

EXHIBIT INDEX

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