

ARBOR REALTY TRUST INC
Form 10-Q
August 05, 2011
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended June 30, 2011

Or

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

For the transition period from _____ to _____

Commission file number: 001-32136

Arbor Realty Trust, Inc.

(Exact name of registrant as specified in its charter)

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Maryland
(State or other jurisdiction of
incorporation)

20-0057959
(I.R.S. Employer
Identification No.)

333 Earle Ovington Boulevard, Suite 900

Uniondale, NY
(Address of principal executive offices)

11553
(Zip Code)

(516) 506-4200

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer
(Do not check if a smaller reporting company)

Smaller reporting company

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. Common stock, \$0.01 par value per share: 25,438,618 outstanding (excluding 1,090,119 shares held in the treasury) as of August 5, 2011.

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ARBOR REALTY TRUST, INC.

FORM 10-Q

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CAUTIONARY STATEMENTS

The information contained in this quarterly report on Form 10-Q is not a complete description of our business or the risks associated with an investment in Arbor Realty Trust, Inc. We urge you to carefully review and consider the various disclosures made by us in this report.

This report contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements relate to, among other things, the operating performance of our investments and financing needs. Forward-looking statements are generally identifiable by use of forward-looking terminology such as may, will, should, potential, intend, expect, endeavor, anticipate, estimate, overestimate, underestimate, believe, could, project, predict, continue or other similar words or expressions. Forward-looking statements are based on certain assumptions, discuss future expectations, describe future plans and strategies, contain projections of results of operations or of financial condition or state other forward-looking information. Our ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Although we believe that the expectations reflected in such forward-looking statements are based on reasonable assumptions, our actual results and performance could differ materially from those set forth in the forward-looking statements. These forward-looking statements involve risks, uncertainties and other factors that may cause our actual results in future periods to differ materially from forecasted results. Factors that could have a material adverse effect on our operations and future prospects include, but are not limited to, changes in economic conditions generally and the real estate market specifically; adverse changes in the financing markets we access affecting our ability to finance our loan and investment portfolio; changes in interest rates; the quality and size of the investment pipeline and the rate at which we can invest our cash; impairments in the value of the collateral underlying our loans and investments; changes in the markets; legislative/regulatory changes; completion of pending investments; the availability and cost of capital for future investments; competition within the finance and real estate industries; and other risks detailed in our Annual Report on Form 10-K for the year ended December 31, 2010. Readers are cautioned not to place undue reliance on any of these forward-looking statements, which reflect our management's views as of the date of this report. The factors noted above could cause our actual results to differ significantly from those contained in any forward-looking statement. For a discussion of our critical accounting policies, see Management's Discussion and Analysis of Financial Condition and Results of Operations of Arbor Realty Trust, Inc. and Subsidiaries Significant Accounting Estimates and Critical Accounting Policies in our Annual Report on Form 10-K for the year ended December 31, 2010.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We are under no duty to update any of the forward-looking statements after the date of this report to conform these statements to actual results.

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****ARBOR REALTY TRUST, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

	June 30, 2011 (Unaudited)	December 31, 2010
Assets:		
Cash and cash equivalents	\$ 42,396,026	\$ 101,124,564
Restricted cash (includes \$63,885,608 and \$21,085,664 from consolidated VIEs, respectively)	65,590,163	21,085,664
Loans and investments, net (includes \$1,144,334,679 and \$1,301,435,584 from consolidated VIEs, respectively)	1,322,526,435	1,414,225,388
Loan held-for-sale	6,160,000	
Available-for-sale securities, at fair value (includes \$2,000,000 and \$1,000,000 from consolidated VIEs, respectively)	4,246,973	3,298,418
Investment in equity affiliates	65,789,451	65,838,885
Real estate owned, net (includes \$86,349,540 and \$2,707,479 from consolidated VIEs, respectively)	151,904,031	22,839,480
Real estate held-for-sale, net	41,440,000	41,440,000
Due from related party (includes \$160,275 and \$335,048 from consolidated VIEs, respectively)	1,994,647	335,048
Prepaid management fee related party	19,047,949	19,047,949
Other assets (includes \$11,777,724 and \$13,645,594 from consolidated VIEs, respectively)	42,538,558	41,972,532
Total assets	\$ 1,763,634,233	\$ 1,731,207,928
Liabilities and Equity:		
Repurchase agreements	\$	\$ 990,997
Collateralized debt obligations (includes \$1,038,328,166 and \$1,070,852,555 from consolidated VIEs, respectively)	1,038,328,166	1,070,852,555
Junior subordinated notes to subsidiary trust issuing preferred securities	158,027,900	157,806,238
Notes payable	85,457,708	51,457,708
Mortgage notes payable real estate owned	74,501,004	20,750,000
Mortgage note payable held-for-sale	41,440,000	41,440,000
Due to related party	1,583,030	17,436,986
Due to borrowers (includes \$1,019,292 and \$1,155,095 from consolidated VIEs, respectively)	1,746,348	2,559,388
Deferred revenue	77,123,133	77,123,133
Other liabilities (includes \$29,654,129 and \$34,940,192 from consolidated VIEs, respectively)	78,367,295	84,375,680
Total liabilities	1,556,574,584	1,524,792,685
Commitments and contingencies		
Equity:		

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Arbor Realty Trust, Inc. stockholders' equity:			
Preferred stock, \$0.01 par value: 100,000,000 shares authorized; no shares issued or outstanding			
Common stock, \$0.01 par value: 500,000,000 shares authorized; 26,423,737 shares issued, 25,408,290 shares outstanding at June 30, 2011 and 25,756,810 shares issued, 24,776,213 shares outstanding at December 31, 2010			
		264,237	257,568
Additional paid-in capital		454,654,595	450,686,382
Treasury stock, at cost	1,015,447 shares at June 30, 2011 and 980,597 shares at December 31, 2010	(10,825,582)	(10,669,585)
Accumulated deficit		(190,784,443)	(180,689,667)
Accumulated other comprehensive loss		(48,184,229)	(55,169,317)
Total Arbor Realty Trust, Inc. stockholders' equity		205,124,578	204,415,381
Noncontrolling interest in consolidated entity		1,935,071	1,999,862
Total equity		207,059,649	206,415,243
Total liabilities and equity		\$ 1,763,634,233	\$ 1,731,207,928

See Notes to Consolidated Financial Statements.

Table of Contents**ARBOR REALTY TRUST, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS**

For the Three and Six Months Ended June 30, 2011 and 2010

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Interest income	\$ 18,572,772	\$ 25,866,947	\$ 36,580,339	\$ 50,085,372
Interest expense	15,792,751	16,177,468	28,833,700	34,264,728
Net interest income	2,780,021	9,689,479	7,746,639	15,820,644
Other revenue:				
Property operating income	8,264,317	815,110	13,684,503	1,028,593
Other income	41,556	224,577	63,432	1,022,624
Total other revenue	8,305,873	1,039,687	13,747,935	2,051,217
Other expenses:				
Employee compensation and benefits	2,285,433	1,995,469	4,373,487	3,900,422
Selling and administrative	1,583,793	2,250,402	2,781,618	3,528,397
Property operating expenses	7,210,374	1,085,143	11,011,595	1,443,573
Depreciation and amortization	1,898,034	134,542	2,330,499	146,710
Other-than-temporary impairment		7,004,800		7,004,800
Impairment loss on real estate owned	750,000		750,000	
Provision for loan losses (net of recoveries)	7,560,263	24,830,000	8,095,398	49,830,000
Loss on restructured loans		825,239	1,000,000	825,239
Management fee - related party	2,050,000	2,000,000	4,000,000	3,900,000
Total other expenses	23,337,897	40,125,595	34,342,597	70,579,141
Loss from continuing operations before gain on extinguishment of debt, loss on sale of securities, net, income (loss) from equity affiliates and provision for income taxes	(12,252,003)	(29,396,429)	(12,848,023)	(52,707,280)
Gain on extinguishment of debt	1,926,700	171,032,651	2,819,200	217,531,130
Loss on sale of securities, net		(10,293,063)		(6,989,583)
Income (loss) from equity affiliates	24,446	(27,348)	48,811	(72,923)
(Loss) income before provision for income taxes	(10,300,857)	131,315,811	(9,980,012)	157,761,344
Provision for income taxes		(1,800,000)		(1,800,000)
(Loss) income from continuing operations	(10,300,857)	129,515,811	(9,980,012)	155,961,344
Loss from discontinued operations		(373,914)		(391,937)
Net (loss) income	(10,300,857)	129,141,897	(9,980,012)	155,569,407
Net income attributable to noncontrolling interest	53,878	53,898	107,574	107,615
Net (loss) income attributable to Arbor Realty Trust, Inc.	\$ (10,354,735)	\$ 129,087,999	\$ (10,087,586)	\$ 155,461,792
Basic (loss) earnings per common share:				
	\$ (0.41)	\$ 5.08	\$ (0.40)	\$ 6.13

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(Loss) income from continuing operations, net of noncontrolling interest							
Loss from discontinued operations			(0.01)				(0.02)
Net (loss) income attributable to Arbor Realty Trust, Inc.	\$	(0.41)	\$	5.07	\$	(0.40)	\$ 6.11
Diluted (loss) earnings per common share:							
(Loss) income from continuing operations, net of noncontrolling interest	\$	(0.41)	\$	5.06	\$	(0.40)	\$ 6.12
Loss from discontinued operations				(0.01)			(0.02)
Net (loss) income attributable to Arbor Realty Trust, Inc.	\$	(0.41)	\$	5.05	\$	(0.40)	\$ 6.10
Dividends declared per common share	\$		\$		\$		\$
Weighted average number of shares of common stock outstanding:							
Basic		25,440,380		25,477,410		25,202,248	25,432,659
Diluted		25,440,380		25,574,203		25,202,248	25,481,323

See Notes to Consolidated Financial Statements.

Table of Contents**ARBOR REALTY TRUST, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**

For the Six Months Ended June 30, 2011

(Unaudited)

	Comprehensive (Loss) Income	Common Stock (1) Shares	Common Stock Par Value	Additional Paid-in Capital	Treasury Stock Shares	Treasury Stock	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Arbor Realty Trust, Inc. Stockholders Equity	Non- controlling Interest	Total
Balance											
January 1, 2011		25,756,810	\$ 257,568	\$ 450,686,382	(980,597)	\$ (10,669,585)	\$ (180,689,667)	\$ (55,169,317)	\$ 204,415,381	\$ 1,999,862	\$ 206,415,243
Issuance of common stock for management fee		666,927	6,669	3,968,213					3,974,882		3,974,882
Purchase of treasury stock					(34,850)	(155,997)			(155,997)		(155,997)
Distributions preferred stock of private REIT							(7,190)		(7,190)		(7,190)
Net (loss) income	\$ (9,980,012)						(10,087,586)		(10,087,586)	107,574	(9,980,012)
Distribution to non-controlling interest										(172,365)	(172,365)
Unrealized gain on securities available-for-sale	970,605							970,605	970,605		970,605
Unrealized loss on derivative financial instruments	(8,403,199)							(8,403,199)	(8,403,199)		(8,403,199)
Reclassification of net realized loss on derivatives designated as cash flow hedges into earnings	14,417,682							14,417,682	14,417,682		14,417,682
Balance June 30, 2011	\$ (2,994,924)	26,423,737	\$ 264,237	\$ 454,654,595	(1,015,447)	\$ (10,825,582)	\$ (190,784,443)	\$ (48,184,229)	\$ 205,124,578	\$ 1,935,071	\$ 207,059,649

(1) Comprehensive income for the six months ended June 30, 2010 was \$144,245,699.

See Notes to Consolidated Financial Statements.

Table of Contents**ARBOR REALTY TRUST, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

For the Six Months Ended June 30, 2011 and 2010

(Unaudited)

	Six Months Ended June 30,	
	2011	2010
Operating activities:		
Net (loss) income	\$ (9,980,012)	\$ 155,569,407
Adjustments to reconcile net (loss) income to net cash (used in) / provided by operating activities:		
Depreciation and amortization	2,330,499	209,853
Stock-based compensation		310,500
Other-than-temporary impairment		7,004,800
Impairment loss on real estate owned	750,000	
Gain on extinguishment of debt	(2,819,200)	(217,531,130)
Loss on sale of securities		6,989,583
Provision for loan losses (net of recoveries)	8,095,398	49,830,000
Loss on restructured loans	1,000,000	825,239
Amortization and accretion of interest and fees	6,834,928	3,757,052
Change in fair value of non-qualifying swaps	557,842	(800,781)
(Income) loss from equity affiliates	(48,811)	72,923
Changes in operating assets and liabilities:		
Other assets	(1,255,270)	730,279
Distributions of operations from equity affiliates	48,811	46,365
Other liabilities	(2,265,131)	2,204,078
Change in restricted cash	(312,465)	
Due to/from related party	(13,619,565)	(297,179)
Net cash (used in) / provided by operating activities	\$ (10,682,976)	\$ 8,920,989
Investing activities:		
Loans and investments funded, originated and purchased, net	(73,028,631)	(12,712,038)
Payoffs and paydowns of loans and investments	67,298,389	77,594,339
Deposits received relating to loan held-for-sale		2,250,000
Proceeds from sale of loans		14,500,000
Due to borrowers and reserves	(732,148)	1,877,887
Change in restricted cash	(1,050,000)	
Deferred fees	1,429,610	212,822
Purchase of securities		(4,481,719)
Principal collection on securities		271,766
Proceeds from sale of available-for-sale securities		50,678,631
Investment in real estate, net	(385,636)	(23,745)
Proceeds from investments in real estate owned, net	2,629,138	
Contributions to equity affiliates		(410,540)
Distributions from equity affiliates	49,434	435,937
Net cash (used in) / provided by investing activities	\$ (3,789,844)	\$ 130,193,340
Financing activities:		

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Proceeds from loan participations and notes payable	30,800,000	26,000,000
Paydowns of mortgage notes payable real estate owned	(1,600,000)	
Payoffs and paydowns of repurchase agreements and notes payable	(990,997)	(160,156,077)
Payoff of junior subordinated notes to subsidiary trust issuing preferred securities		(10,500,122)
Proceeds from collateralized debt obligations	2,357,959	5,500,000
Payoffs and paydowns of collateralized debt obligations	(31,693,684)	(39,936,209)
Change in restricted cash	(42,799,944)	3,075,122
Payments on swaps to hedge counterparties	(9,670,000)	(13,440,000)
Receipts on swaps from hedge counterparties	9,810,000	8,370,000
Purchases of treasury stock	(155,997)	
Distributions paid to noncontrolling interest	(172,365)	(108,940)
Distributions paid on preferred stock of private REIT	(7,190)	(7,190)
Payment of deferred financing costs	(133,500)	(411,381)
Net cash used in financing activities	\$ (44,255,718)	\$ (181,614,797)
Net decrease in cash and cash equivalents	\$ (58,728,538)	\$ (42,500,468)
Cash and cash equivalents at beginning of period	101,124,564	64,624,275
Cash and cash equivalents at end of period	\$ 42,396,026	\$ 22,123,807

See Notes to Consolidated Financial Statements.

Table of Contents**ARBOR REALTY TRUST, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)**

For the Six Months Ended June 30, 2011 and 2010

(Unaudited)

	Six Months Ended June 30,	
	2011	2010
Supplemental cash flow information:		
Cash used to pay interest	\$ 21,364,179	\$ 29,020,708
Cash used for taxes	\$ 290,090	\$ 371,879
Supplemental schedule of non-cash investing and financing activities:		
Loans transferred to real estate owned, net	\$ 83,099,540	\$ 20,750,000
Assumption of mortgage note payable real estate owned	\$ 55,351,004	\$ 20,750,000
Issuance of common stock for management incentive fee	\$ 3,974,882	\$
Extinguishment of notes payable	\$	\$ 159,417,756
Extinguishment of trust preferred securities	\$	\$ 102,110,610
Re-issuance of CDO debt	\$	\$ 42,304,391
Accrual of interest on reissued collateralized debt obligations	\$	\$ 22,941,851
Available-for-sale securities exchanged	\$	\$ 400,000
Investments transferred to available-for-sale securities, at fair value	\$	\$ 35,814,344
Loan payoffs and paydowns received by related party	\$	\$ 14,505,791

See Notes to Consolidated Financial Statements.

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ARBOR REALTY TRUST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2011

(Unaudited)

Note 1 Description of Business/Form of Ownership

Arbor Realty Trust, Inc. (the Company) is a Maryland corporation that was formed in June 2003 to invest in a diversified portfolio of multi-family and commercial real estate related assets, primarily consisting of bridge loans, mezzanine loans, junior participating interests in first mortgage loans, and preferred and direct equity. The Company may also directly acquire real property and invest in real estate-related notes and certain mortgage-related securities. The Company conducts substantially all of its operations through its operating partnership, Arbor Realty Limited Partnership (ARLP), and ARLP's wholly-owned subsidiaries. The Company is externally managed and advised by Arbor Commercial Mortgage, LLC (ACM).

The Company is organized and conducts its operations to qualify as a real estate investment trust (REIT) for federal income tax purposes. A REIT is generally not subject to federal income tax on its REIT taxable income that it distributes to its stockholders, provided that it distributes at least 90% of its REIT taxable income and meets certain other requirements. Certain assets of the Company that produce non-qualifying income are owned by its taxable REIT subsidiaries, the income of which is subject to federal and state income taxes.

The Company's charter provides for the issuance of up to 500 million shares of common stock, par value \$0.01 per share, and 100 million shares of preferred stock, par value \$0.01 per share. The Company was incorporated in June 2003 and was initially capitalized through the sale of 67 shares of common stock for \$1,005.

On July 1, 2003, ACM contributed \$213.1 million of structured finance assets and \$169.2 million of borrowings supported by \$43.9 million of equity in exchange for a commensurate equity ownership in ARLP. In addition, certain employees of ACM were transferred to ARLP. At that time, these assets, liabilities and employees represented a substantial portion of ACM's structured finance business. The Company is externally managed and advised by ACM and pays ACM a management fee in accordance with a management agreement. ACM also sources originations, provides underwriting services and services all structured finance assets on behalf of ARLP, and its wholly owned subsidiaries.

On July 1, 2003, the Company completed a private equity offering of 1,610,000 units (including an overallotment option), each consisting of five shares of common stock and one warrant to purchase one share of common stock at \$75.00 per unit. The Company sold 8,050,000 shares of common stock in the offering. Gross proceeds from the private equity offering totaled \$120.2 million. Gross proceeds from the private equity offering combined with the concurrent equity contribution by ACM totaled approximately \$164.1 million in equity capital. The Company paid and accrued offering expenses of \$10.1 million resulting in Arbor Realty Trust, Inc. stockholders' equity and noncontrolling interest of \$154.0 million as a result of the private placement.

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In April 2004, the Company sold 6,750,000 shares of its common stock in a public offering at a price of \$20.00 per share, for net proceeds of approximately \$124.4 million after deducting the underwriting discount and other estimated offering expenses. The Company used the proceeds to pay down indebtedness. In May 2004, the underwriters exercised a portion of their over-allotment option, which resulted in the issuance of 524,200 additional shares. The Company received net proceeds of approximately \$9.8 million after deducting the underwriting discount. In October 2004, ARLP received proceeds of approximately \$9.4 million from the exercise of warrants for 629,345 operating partnership units. Additionally, in 2004 and 2005, the Company issued 973,354 and 282,776 shares of common stock, respectively, from the exercise of warrants under its Warrant Agreement dated July 1, 2003, the (Warrant Agreement) and received net proceeds of \$12.9 million and \$4.2 million, respectively.

In June 2007, the Company completed a public offering in which it sold 2,700,000 shares of its common stock registered for \$27.65 per share, and received net proceeds of approximately \$73.6 million after deducting the underwriting discount and the other estimated offering expenses. The Company used the proceeds to pay down debt and finance its loan and investment portfolio.

In June 2008, the Company's external manager exercised its right to redeem its approximate 3.8 million operating partnership units in the Company's operating partnership for shares of the Company's common stock on a

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ARBOR REALTY TRUST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2011

(Unaudited)

one-for-one basis. In addition, the special voting preferred shares paired with each operating partnership unit, pursuant to a pairing agreement, were redeemed simultaneously and cancelled by the Company.

In June 2010, the Company filed a shelf registration statement on Form S-3 with the Securities and Exchange Commission (SEC) under the Securities Act of 1933, as amended (the 1933 Act) with respect to an aggregate of \$500.0 million of debt securities, common stock, preferred stock, depositary shares and warrants that may be sold by the Company from time to time pursuant to Rule 415 of the 1933 Act. On June 23, 2010, the SEC declared this shelf registration statement effective.

The Company had 25,408,290 shares of common stock outstanding at June 30, 2011 and 24,776,213 shares of common stock outstanding at December 31, 2010.

Note 2 Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

The accompanying unaudited consolidated interim financial statements have been prepared in accordance with the Financial Accounting Standards Board (FASB) Accounting Standards Codification , the authoritative reference for accounting principles generally accepted in the United States (GAAP), for interim financial statements and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements, although management believes that the disclosures presented herein are adequate to prevent the accompanying unaudited consolidated interim financial statements presented from being misleading.

The accompanying unaudited consolidated financial statements include the financial statements of the Company, its wholly owned subsidiaries, partnerships or other joint ventures in which the Company owns a voting interest of greater than 50 percent, and Variable Interest Entities (VIEs) of which the Company is the primary beneficiary. VIEs are defined as entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. A VIE is required to be consolidated by its primary beneficiary, which is the party that (i) has the power to control the activities that most significantly impact the VIE's economic performance and (ii) has the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. Updated accounting guidance requires the Company to present a) assets of a consolidated VIE that can be used only to settle obligations of the consolidated VIE, and b) liabilities of a consolidated VIE for which creditors (or beneficial interest holders) do not have recourse to the general

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credit of the primary beneficiary. As a result of this guidance, the Company has separately disclosed parenthetically the assets and liabilities of its three collateralized debt obligation (CDO) subsidiaries on its Consolidated Balance Sheets. Entities in which the Company owns a voting interest of 20 percent to 50 percent are accounted for primarily under the equity method.

In the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included. All significant inter-company transactions and balances have been eliminated in consolidation. Certain prior year amounts have been reclassified to conform to current period presentation. One of the Company's real estate investments was reclassified from real estate owned to real estate held-for-sale at September 30, 2010, and was subsequently sold in October 2010, which resulted in a reclassification of its operating activity from property operating income and expenses to discontinued operations for all prior period presentations.

The preparation of consolidated interim financial statements in conformity with GAAP requires management to make estimates and assumptions in determining the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Interim Financial Statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Further, in connection with preparation of the Consolidated Interim Financial Statements, the Company

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(Unaudited)

evaluated events subsequent to the balance sheet date of June 30, 2011 through the issuance of the Consolidated Financial Statements.

The results of operations for the three and six months ended June 30, 2011 are not necessarily indicative of results that may be expected for the entire year ending December 31, 2011. The accompanying unaudited consolidated interim financial statements should be read in conjunction with the Company's audited consolidated annual financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2010.

Cash and Cash Equivalents

All highly liquid investments with original maturities of three months or less are considered to be cash equivalents. The Company places its cash and cash equivalents in high quality financial institutions. The consolidated account balances at each institution periodically exceed Federal Deposit Insurance Corporation (FDIC) insurance coverage and the Company believes that this risk is not significant.

Restricted Cash

At June 30, 2011 and December 31, 2010, the Company had restricted cash of \$65.6 million and \$21.1 million, respectively. Restricted cash primarily represents proceeds from loan repayments on deposit with the trustees for the Company's CDOs which will be used to purchase replacement loans as collateral for the CDO that has not reached its replenishment date, unfunded loan commitments, interest payments received from loans and principal repayments for the CDOs that have reached their replenishment dates, and are remitted quarterly to the bond holders and the Company in the month following the quarter. See Note 7 Debt Obligations. One of the Company's recently acquired real estate owned assets also has a restricted cash balance of \$1.7 million as of June 30, 2011 due to a first mortgage escrow requirement. See Note 6 Real Estate Owned and Held-For-Sale.

Loans, Investments and Securities

At the time of purchase, the Company designates a security as held-to-maturity, available-for-sale, or trading depending on the Company's ability and intent to hold it to maturity. The Company does not have any securities designated as trading or held-to-maturity as of June 30, 2011. Securities available-for-sale are reported at fair value with the net unrealized gains or losses reported as a component of accumulated other

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comprehensive loss. Unrealized losses that are determined to be other-than-temporary are recognized in earnings up to their credit component. The determination of other-than-temporary impairment is a subjective process requiring judgments and assumptions. The process may include, but is not limited to, assessment of recent market events and prospects for near-term recovery, assessment of cash flows, internal review of the underlying assets securing the investments, credit of the issuer and the rating of the security, as well as the Company's ability and intent to hold the investment to maturity. Management closely monitors market conditions on which it bases such decisions.

The Company also assesses certain of its securities, other than those of high credit quality, to determine whether significant changes in estimated cash flows or unrealized losses on these securities, if any, reflect a decline in value which is other-than-temporary and, accordingly, should be written down to their fair value against earnings. On a quarterly basis, the Company reviews these changes in estimated cash flows, which could occur due to actual prepayment and credit loss experience, to determine if an other-than-temporary impairment is deemed to have occurred. The determination of other-than-temporary impairment is a subjective process requiring judgments and assumptions and is not necessarily intended to indicate a permanent decline in value. The Company calculates a revised yield based on the current amortized cost of the investment, including any other-than-temporary impairments recognized to date, and the revised yield is then applied prospectively to recognize interest income.

Loans held for investment are intended to be held to maturity and, accordingly, are carried at cost, net of unamortized loan origination costs and fees, loan purchase discounts, and net of the allowance for loan losses when such loan or investment is deemed to be impaired. The Company invests in preferred equity interests that, in some cases, allow the Company to participate in a percentage of the underlying property's cash flows from operations and

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proceeds from a sale or refinancing. At the inception of each such investment, management must determine whether such investment should be accounted for as a loan, joint venture or as real estate. To date, management has determined that all such investments are properly accounted for and reported as loans.

From time to time the Company may enter into an agreement to sell a loan. These loans are considered held-for-sale and are valued at the lower of the loan's carrying amount or fair value less costs to sell. For the sale of loans, recognition occurs when ownership passes to the buyer.

Impaired Loans, Allowance for Loan Losses, Loss on Restructured Loans and Charge-offs

The Company considers a loan impaired when, based upon current information and events, it is probable that it will be unable to collect all amounts due for both principal and interest according to the contractual terms of the loan agreement. The Company evaluates each loan in its portfolio on a quarterly basis. The Company's loans are individually specific and unique as it relates to product type, geographic location, and collateral type, as well as to the rights and remedies and the position in the capital structure the Company's loans and investments have in relation to the underlying collateral. The Company evaluates all of this information as well as general market trends related to specific classes of assets, collateral type and geographic locations, when determining the appropriate assumptions such as capitalization and market discount rates, as well as the borrower's operating income and cash flows, in estimating the value of the underlying collateral when determining if a loan is impaired. The Company utilizes internally developed valuation models and techniques primarily consisting of discounted cash flow and direct capitalization models in determining the fair value of the underlying collateral on an individual loan. The Company may also obtain a third party appraisal, which may include as-is or stabilized value. Such appraisals may be used as an additional source of valuation information only and no adjustments are made to appraisals. Included in the evaluation of the capitalization and market discount rates, the Company considers not only assumptions specific to the collateral but also considers geographical and industry trends that could impact the collateral's value.

If upon completion of the valuation, the fair value of the underlying collateral securing the impaired loan is less than the net carrying value of the loan, an allowance is created with a corresponding charge to the provision for loan losses. The allowance for each loan is maintained at a level that is believed to be adequate by management to absorb probable losses. The Company had an allowance for loan losses of \$171.2 million relating to 26 loans with an aggregate carrying value, before reserves, of approximately \$318.9 million at June 30, 2011 and \$205.5 million in allowance for loan losses relating to 30 loans with an aggregate carrying value, before reserves, of approximately \$530.6 million at December 31, 2010. In addition, during the second quarter of 2011, the Company recorded net recoveries of \$3.8 million related to five loans in the Company's portfolio. During the first quarter of 2011, the Company recorded recoveries of \$1.0 million related to two loans in the Company's portfolio. These recoveries were recorded in provision for loan losses on the Consolidated Statement of Operations.

Loan terms may be modified if the Company determines that based on the individual circumstances of a loan and the underlying collateral, a modification would more likely increase the total recovery of combined principal and interest recovery from the loan. Any loan modification is

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predicated upon a goal of maximizing the collection of the loan. Typical triggers for a modification would include situations where the projected cash flow is insufficient to cover required debt service, when asset performance is lagging the initial projections, where there is a requirement for rebalancing, where there is an impending maturity of the loan, and where there is an actual loan default. Loan terms that have been modified have included, but are not limited to interest rate, maturity date and in certain cases, principal amount. Length and amounts of each modification have varied based on individual circumstances and are determined on a case by case basis. If the loan modification constitutes a concession whereas the Company does not receive ample consideration in return for the modification, and the borrower is experiencing financial difficulties and cannot repay the loan under the current terms, then the modification is considered by the Company to be a troubled debt restructuring. If the Company receives a benefit, either monetary or strategic, and the above criteria are not met, the modification is not considered to be a troubled debt restructuring.

The Company records interest on modified loans on an accrual basis to the extent that the modified loan is contractually current. To date, the Company has not recorded interest income on a modified loan where the Company has not subsequently received the cash.

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Loss on restructured loans are recorded when the Company has granted a concession to the borrower in the form of principal forgiveness related to the payoff or the substitution or addition of a new debtor for the original borrower or when the Company incurs costs on behalf of the borrower related to the modification, payoff or the substitution or addition of a new debtor for the original borrower. When a loan is restructured, the Company records its investment at net realizable value, taking into account the cost of all concessions at the date of restructuring. The reduction in the recorded investment is recorded as a charge to the Statement of Operations in the period in which the loan is restructured. The Company recorded a loss on restructured loans of \$1.0 million for the six months ended June 30, 2011 as a result of the execution of a forbearance agreement in the first quarter of 2011 on a loan modified in the second quarter of 2011. For the three and six months ended June 30, 2010, the Company recorded a loss on restructured loans of \$0.8 million.

Charge-offs to the allowance for loan losses occur when losses are confirmed through the receipt of cash or other consideration from the completion of a sale; when a modification or restructuring takes place in which the Company grants a concession to a borrower or agrees to a discount in full or partial satisfaction of the loan; when the Company takes ownership and control of the underlying collateral in full satisfaction of the loan; when loans are reclassified as other investments; or when significant collection efforts have ceased and it is highly likely that a loss has been realized. For the six months ended June 30, 2011 and 2010, the Company recorded charge-offs to the allowance for loan losses of \$45.3 million and \$46.4 million, respectively.

Real Estate Owned and Held-For-Sale

Real estate owned, shown net of accumulated depreciation and impairment charges, is comprised of real property acquired by foreclosure or through partial or full settlement of mortgage debt. The real estate acquired is recorded at the estimated fair value at the time of acquisition.

Costs incurred in connection with the foreclosure of the properties collateralizing the real estate loans are expensed as incurred and costs subsequently incurred to extend the life or improve the assets subsequent to foreclosure are capitalized.

The Company allocates the purchase price of operating properties to land, building, tenant improvements, deferred lease cost for the origination costs of the in-place leases, intangibles for the value of the above or below market leases at fair value and to any other identified intangible assets or liabilities. The Company finalizes its purchase price allocation on these assets within one year of the acquisition date. The Company amortizes the value allocated to the in-place leases over the remaining lease term. The value allocated to the above or below market leases are amortized over the remaining lease term as an adjustment to rental income.

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Real estate assets, including assets acquired by foreclosure or through partial or full settlement of mortgage debt, that are operated for the production of income are depreciated using the straight-line method over their estimated useful lives. Ordinary repairs and maintenance which are not reimbursed by the tenants are expensed as incurred. Major replacements and betterments which improve or extend the life of the asset are capitalized and depreciated over their estimated useful life.

The Company's properties are individually reviewed for impairment each quarter, if events or circumstances change indicating that the carrying amount of the assets may not be recoverable. The Company recognizes impairment if the undiscounted estimated cash flows to be generated by the assets are less than the carrying amount of those assets. Measurement of impairment is based upon the estimated fair value of the asset. Upon evaluating a property for impairment, many factors are considered, including estimated current and expected operating cash flows from the property during the projected holding period, costs necessary to extend the life or improve the asset, expected capitalization rates, projected stabilized net operating income, selling costs, and the ability to hold and dispose of such real estate owned in the ordinary course of business. Valuation adjustments may be necessary in the event that effective interest rates, rent-up periods, future economic conditions, and other relevant factors vary significantly from those assumed in valuing the property. If future evaluations result in a diminution in the value of the property, the reduction will be recognized as an impairment charge at that time.

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Real estate is classified as held-for-sale when management commits to a plan of sale, the asset is available for immediate sale, there is an active program to locate a buyer, and it is probable the sale will be completed within one year. Properties classified as held-for-sale are not depreciated and the results of their operations are shown in discontinued operations. Real estate assets that are expected to be disposed of are valued, on an individual asset basis, at the lower of their carrying amount or their fair value less costs to sell.

The Company recognizes sales of real estate properties upon closing. Payments received from purchasers prior to closing are recorded as deposits. Profit on real estate sold is recognized upon closing using the full accrual method when the collectability of the sale price is reasonably assured and the Company is not obligated to perform significant activities after the sale. Profit may be deferred in whole or in part until collectability of the sales price is reasonably assured and the earnings process is complete.

Revenue Recognition

Interest income Interest income is recognized on the accrual basis as it is earned from loans, investments, and securities. In certain instances, the borrower pays an additional amount of interest at the time the loan is closed, an origination fee, a prepayment fee and/or deferred interest upon maturity. In some cases, interest income may also include the amortization or accretion of premiums and discounts arising from the purchase or origination of the loan or security. This additional income, net of any direct loan origination costs incurred, is deferred and accreted into interest income on an effective yield or interest method adjusted for actual prepayment activity over the life of the related loan or security as a yield adjustment. Income recognition is suspended for loans when, in the opinion of management, a full recovery of all contractual principal is not probable. Income recognition is resumed when the loan becomes contractually current and performance is resumed. The Company records interest income on certain impaired loans to the extent cash is received, in which a loan loss reserve has been recorded, as the borrower continues to make interest payments. The Company recorded loan loss reserves related to these loans as it was deemed that full recovery of principal and interest was not probable.

Several of the Company's loans provide for accrual of interest at specified rates, which differ from current payment terms. Interest is recognized on such loans at the accrual rate subject to management's determination that accrued interest and outstanding principal are ultimately collectible, based on the underlying collateral and operations of the borrower. If management cannot make this determination, interest income above the current pay rate is recognized only upon actual receipt. The Company currently has no loans in its portfolio accruing such interest. Therefore, interest income is recorded on all of the Company's loans and investments only to the extent that the current pay rate is received.

Given the transitional nature of some of the Company's real estate loans, the Company may require funds to be placed into an interest reserve, based on contractual requirements, to cover debt service costs. The Company will analyze these interest reserves on a periodic basis and determine if any additional interest reserves are needed. Recognition of income on loans with funded interest reserves are accounted for in the same manner as loans without funded interest reserves. The Company will not recognize any interest income on loans in which the borrower has

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failed to make the contractual interest payment due or has not replenished the interest reserve account. As of June 30, 2011, the Company had total interest reserves of \$7.6 million on 31 loans with an aggregate unpaid principal balance of \$551.6 million and had three non-performing loans with an aggregate unpaid principal balance of \$44.3 million with a funded interest reserve of \$0.1 million. Income from non-performing loans is generally recognized on a cash basis only to the extent it is received. Full income recognition will resume when the loan becomes contractually current and performance has recommenced.

Additionally, interest income is recorded when earned from equity participation interests, referred to as equity kickers. These equity kickers have the potential to generate additional revenues to the Company as a result of excess cash flow distributions and/or as appreciated properties are sold or refinanced. The Company did not record interest income from such investments for the three and six month periods ended June 30, 2011 and 2010, respectively.

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Property operating income Property operating income represents income associated with the operations of commercial real estate properties classified as real estate owned. The Company recognizes revenue for these activities when the fees are fixed or determinable, or are evidenced by an arrangement, collection is reasonably assured and the services under the arrangement have been provided. For the three and six months ended June 30, 2011, the Company recorded approximately \$8.3 million and \$13.7 million, respectively, of property operating income relating to its real estate owned properties, as compared to approximately \$0.8 million and \$1.0 million, respectively, for the three and six months ended June 30, 2010. As of June 30, 2011, the Company had four real estate owned properties including a portfolio of multifamily assets that was purchased by the Company out of bankruptcy and a portfolio of hotel assets that was transferred to the Company by the owner, a creditor trust. Both of these portfolios were acquired in the first quarter of 2011. As of June 30, 2010, the Company had two real estate owned properties. Additionally, another real estate investment was reclassified from real estate owned to real estate held-for-sale in the third quarter of 2010, which resulted in a reclassification of its operating activity from property operating income and expenses into discontinued operations for all prior periods. See Note 6 Real Estate Owned and Held-For-Sale for further details.

Other income Other income represents loan structuring, defeasance, and miscellaneous asset management fees associated with the Company's loans and investments portfolio. The Company recognizes these forms of income when the fees are fixed or determinable, are evidenced by an arrangement, collection is reasonably assured and the services under the arrangement have been provided.

Investment in Equity Affiliates

The Company invests in joint ventures that are formed to acquire, develop, and/or sell real estate assets. These joint ventures are not majority owned or controlled by the Company, or are VIEs for which the Company is not the primary beneficiary, and are not consolidated in its financial statements. These investments are recorded under either the equity or cost method of accounting as appropriate. The Company records its share of the net income and losses from the underlying properties of its equity method investments and any other-than-temporary impairment on these investments on a single line item in the Consolidated Statements of Operations as income or losses from equity affiliates.

Stock-Based Compensation

The Company has granted certain of its employees, independent directors, and employees of ACM, restricted stock awards consisting of shares of the Company's common stock that vest immediately or annually over a multi-year period, subject to the recipient's continued service to the Company. The Company records stock-based compensation expense at the grant date fair value of the related stock-based award with subsequent remeasurement for any unvested shares granted to non-employees of the Company with such amounts expensed against earnings, at the grant date (for the portion that vest immediately) or ratably over the respective vesting periods. Dividends are paid on the restricted stock as dividends are paid on shares of the Company's common stock whether or not they are vested. Stock-based compensation is disclosed in the Company's Consolidated Statements of Operations under employee compensation and benefits for employees and under selling and

administrative expense for non-employees.

Income Taxes

The Company is organized and conducts its operations to qualify as a REIT and to comply with the provisions of the Internal Revenue Code with respect thereto. A REIT is generally not subject to federal income tax on taxable income which is distributed to its stockholders, provided that the Company distributes at least 90% of its taxable income and meets certain other requirements. Certain REIT income may be subject to state and local income taxes. The Company's assets or operations that would not otherwise comply with the REIT requirements, are owned or conducted by the Company's taxable REIT subsidiaries, the income of which is subject to federal and state income tax. Under current federal tax law, the income and the tax on such income, if any, attributable to certain debt extinguishment transactions realized in 2009 and 2010 may, at the Company's election, be deferred to future periods.

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Current accounting guidance clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements. This guidance prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This guidance also provides clarity on derecognition, classification, interest and penalties, accounting in interim periods and disclosure.

Other Comprehensive Income / (Loss)

The Company divides comprehensive income or loss into net income (loss) and other comprehensive income (loss), which includes unrealized gains and losses on available-for-sale securities. In addition, to the extent the Company's derivative instruments qualify as hedges, net unrealized gains or losses are reported as a component of accumulated other comprehensive income/(loss). See *Derivatives and Hedging Activities* below. At June 30, 2011, accumulated other comprehensive loss was \$48.2 million and consisted of \$49.3 million of net unrealized losses on derivatives designated as cash flow hedges and a \$1.1 million unrealized gain related to available-for-sale securities. At December 31, 2010, accumulated other comprehensive loss was \$55.2 million and consisted of \$55.3 million of net unrealized losses on derivatives designated as cash flow hedges and a \$0.1 million unrealized gain related to available-for-sale securities.

Derivatives and Hedging Activities

The Company recognizes all derivatives as either assets or liabilities at fair value and these amounts are recorded in other assets or other liabilities on the Consolidated Balance Sheets. Additionally, the fair value adjustments will affect either accumulated other comprehensive income (loss) until the hedged item is recognized in earnings, or net income (loss) depending on whether the derivative instrument qualifies as a hedge for accounting purposes and, if so, the nature of the hedging activity. The Company utilizes quotations from a third party to assist in the determination of these fair values.

The Company records all derivatives on the Consolidated Balance Sheets at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether a company has elected to designate a derivative in a hedging relationship and apply hedge accounting and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. Derivatives designated and qualifying as a hedge of the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives designated and qualifying as a hedge of the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. Hedge accounting generally provides for the matching of the timing of gain or loss recognition on the hedging instrument with the recognition of the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk in a fair value hedge or the earnings effect of the hedged forecasted transactions in a cash flow hedge. The Company may enter into derivative contracts that are intended to economically hedge certain of its risks, even though hedge accounting does not apply or the Company elects not to apply hedge accounting.

In the normal course of business, the Company may use a variety of derivative financial instruments to manage, or hedge, interest rate risk. These derivative financial instruments must be effective in reducing its interest rate risk exposure in order to qualify for hedge accounting. When the terms of an underlying transaction are modified, or when the underlying hedged item ceases to exist, all changes in the fair value of the instrument are marked-to-market with changes in value included in net income (loss) for each period until the derivative instrument matures or is settled. In cases where a derivative financial instrument is terminated early, any gain or loss is generally amortized over the remaining life of the hedged item. Any derivative instrument used for risk management that does not meet the hedging criteria is marked-to-market with the changes in value included in net income (loss). The Company uses derivatives for hedging purposes rather than speculation. See Note 8 Derivative Financial Instruments for further details.

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Variable Interest Entities

The Company has evaluated its loans and investments, mortgage related securities, investments in equity affiliates, junior subordinated notes and CDOs, in order to determine if they qualify as VIEs or as variable interests in VIEs. This evaluation resulted in the Company determining that its bridge loans, junior participation loans, mezzanine loans, preferred equity investments, investments in equity affiliates, junior subordinated notes, CDOs, and investments in debt securities were potential VIEs or variable interests in VIEs. A VIE is defined as an entity in which equity investors (i) do not have the characteristics of a controlling financial interest, and/or (ii) do not have sufficient equity at risk for the entity to finance its activities without additional financial support from other parties. A VIE is required to be consolidated by its primary beneficiary, which is defined as the party that (i) has the power to control the activities that most significantly impact the VIE's economic performance and (ii) has the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. See Note 9 Variable Interest Entities for further details.

Recently Issued Accounting Pronouncements

In June 2011, the FASB issued updated guidance on comprehensive income which amends U.S. GAAP to conform to the disclosure requirements of International Financial Reporting Standards (IFRS). The amendment eliminates the option to present components of other comprehensive income as part of the Statement of Changes in Stockholders' Equity and requires a separate Statement of Comprehensive Income or two consecutive statements in the Statement of Operations and in a separate Statement of Comprehensive Income. This guidance is effective as of the first quarter of 2012, though early adoption is permitted, and its adoption is not expected to have a material effect on the Company's Consolidated Financial Statements.

In May 2011, the FASB issued updated guidance on fair value measurement which amends U.S. GAAP to conform to IFRS measurement and disclosure requirements. The amendments change the wording used to describe the requirements in U.S. GAAP for measuring fair value, changes certain fair value measurement principles and enhances disclosure requirements. This guidance is effective as of the first quarter of 2012, applied prospectively, and its adoption is not expected to have a material effect on the Company's Consolidated Financial Statements.

In April 2011, the FASB issued updated guidance on a creditor's determination of whether a restructuring will be a troubled debt restructuring, which establishes new guidelines in evaluating whether a loan modification meets the criteria of a troubled debt restructuring. This guidance is effective as of the third quarter of 2011, applied retrospectively to the beginning of the fiscal year as required, and its adoption is not expected to have a material effect on the Company's Consolidated Financial Statements.

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In December 2010, the FASB issued updated guidance on business combinations, which clarifies that when pro forma financial information is required, it is to be presented as if the business combination occurred at the beginning of the prior year. The guidance also requires a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination. The guidance is effective for business combinations in fiscal years beginning on or after December 15, 2010 and the adoption of this guidance on January 1, 2011 did not have a material effect on the Company's Consolidated Financial Statements.

In July 2010, the FASB issued updated guidance on disclosures about the credit quality of financing receivables and the allowance for credit losses which requires a greater level of information disclosed about the credit quality of loans and allowance for loan losses, as well as additional information related to credit quality indicators, past due information, and information related to loans modified in a troubled debt restructuring. This guidance is effective as of the fourth quarter of 2010, except for the information related to loans modified in a troubled debt restructuring which was postponed by the FASB to the third quarter of 2011. As the guidance only amends existing disclosure requirements, its adoption resulted in additional disclosures and did not have a material effect on the Company's Consolidated Financial Statements.

In January 2010, the FASB issued updated guidance on fair value measurements and disclosures, which requires disclosure of details of significant asset or liability transfers in and out of Level 1 and Level 2 measurements within the fair value hierarchy and inclusion of gross purchases, sales, issuances, and settlements in

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the roll forward of assets and liabilities valued using Level 3 inputs within the fair value hierarchy. The guidance also clarifies and expands existing disclosure requirements related to the disaggregation of fair value disclosures and inputs used in arriving at fair values for assets and liabilities using Level 2 and Level 3 inputs within the fair value hierarchy. This guidance is effective for interim and annual reporting periods beginning after December 15, 2009, and its adoption did not have a material effect on the Company's Consolidated Financial Statements. The gross presentation of the Level 3 roll forward is required for interim and annual reporting periods beginning after December 15, 2010 and its adoption on January 1, 2011 did not have a material effect on the Company's Consolidated Financial Statements.

Note 3 Loans and Investments

The following table sets forth the composition of the Company's loan and investment portfolio at June 30, 2011 and December 31, 2010:

	June 30, 2011 (1)	Percent of Total	Loan Count	Wtd. Avg. Pay Rate (2)	Wtd. Avg. Remaining Months to Maturity	First Dollar LTV Ratio (3)	Last Dollar LTV Ratio (4)
Bridge loans	\$ 899,146,004	59%	54	4.48%	31.2	0%	85%
Mezzanine loans	196,413,974	13%	28	4.47%	37.5	79%	98%
Junior participation loans	328,014,030	22%	11	4.34%	43.2	65%	85%
Preferred equity investments	90,586,631	6%	18	2.83%	65.9	89%	98%
	1,514,160,639	100%	111	4.35%	36.7	29%	87%
Unearned revenue	(14,242,839)						
Allowance for loan losses	(171,231,365)						
Loans and investments, net	\$ 1,328,686,435						

	December 31, 2010 (1)	Percent of Total	Loan Count	Wtd. Avg. Pay Rate (2)	Wtd. Avg. Remaining Months to Maturity	First Dollar LTV Ratio (3)	Last Dollar LTV Ratio (4)
Bridge loans	\$ 1,070,013,851	66%	54	4.14%	33.0	0%	88%
Mezzanine loans	233,406,411	14%	30	4.83%	32.4	78%	97%
Junior participation loans	240,971,047	15%	12	5.15%	41.5	61%	86%
Preferred equity investments	89,472,959	5%	17	5.68%	72.3	90%	98%
	1,633,864,268	100%	113	4.47%	36.3	30%	89%
Unearned revenue	(14,168,578)						
Allowance for loan losses	(205,470,302)						

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Loans and investments, net \$ 1,414,225,388

- (1) Includes a bridge loan with an unpaid principal balance of \$6.2 million as of June 30, 2011 classified as held-for-sale due to the Company's intent to sell the loan within one year. There were no loans classified as held-for-sale as of December 31, 2010.
- (2) The Weighted Average Pay Rate is a weighted average, based on the unpaid principal balances of each loan in the Company's portfolio, of the interest rate that is required to be paid monthly as stated in the individual loan agreements. Certain loans and investments that require an additional rate of interest Accrual Rate to be paid at the maturity are not included in the weighted average pay rate as shown in the table. At June 30, 2011 and December 31, 2010 the Company had no such loans in its portfolio that were currently accruing such interest.
- (3) The First Dollar LTV Ratio is calculated by comparing the total of the Company's senior most dollar and all senior lien positions within the capital stack to the fair value of the underlying collateral to determine the point at which the Company will absorb a total loss of its position.
- (4) The Last Dollar LTV Ratio is calculated by comparing the total of the carrying value of the Company's loan and all senior lien positions within the capital stack to the fair value of the underlying collateral to determine the point at which the Company will initially absorb a loss.

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ARBOR REALTY TRUST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2011

(Unaudited)

Concentration of Credit Risk

The Company operates in one portfolio segment, commercial mortgage loans and investments. Commercial mortgage loans and investments can potentially subject the Company to concentrations of credit risk. The Company is subject to concentration risk in that, as of June 30, 2011, the unpaid principal balance related to 26 loans with five unrelated borrowers represented approximately 28% of total assets. At December 31, 2010 the unpaid principal balance related to 32 loans with five unrelated borrowers represented approximately 32% of total assets. As of June 30, 2011 and December 31, 2010, the Company had 111 and 113 loans and investments, respectively.

As a result of the loan review process, the Company identified loans and investments that it considers higher-risk loans that had a carrying value, before loan loss reserves, of approximately \$329.7 million and a weighted average last dollar loan-to-value (LTV) ratio of 97%, compared to lower-risk loans with a carrying value, before loan loss reserves, of \$1.2 billion and a weighted average last dollar LTV ratio of 85% at June 30, 2011.

The Company measures its relative loss position for its mezzanine loans, junior participation loans, and preferred equity investments by determining the point where the Company will be exposed to losses based on its position in the capital stack as compared to the fair value of the underlying collateral. The Company determines its loss position on both a first dollar LTV and a last dollar LTV basis. First dollar LTV is calculated by comparing the total of the Company's senior most dollar and all senior lien positions within the capital stack to the fair value of the underlying collateral to determine the point at which the Company will absorb a total loss of its position. Last dollar LTV is calculated by comparing the total of the carrying value of the Company's loan and all senior lien positions within the capital stack to the fair value of the underlying collateral to determine the point at which the Company will initially absorb a loss.

As a component of the Company's policies and procedures for loan valuation and risk assessment, each loan and investment is assigned a credit risk rating. Individual ratings range from one to five, with one being the lowest risk and five being the highest. Each credit risk rating has benchmark guidelines which pertain to debt-service coverage ratios, LTV ratios, borrower strength, asset quality, and funded cash reserves. Other factors such as guarantees, market strength, remaining loan term, and borrower equity are also reviewed and factored into determining the credit risk rating assigned to each loan. This metric provides a helpful snapshot of portfolio quality and credit risk. Given the Company's asset management approach, however, the risk rating process does not result in differing levels of diligence contingent upon credit rating. That is because all portfolio assets are subject to the level of scrutiny and ongoing analysis consistent with that of a high-risk loan. All assets are subject to, at minimum, a thorough quarterly financial evaluation in which historical operating performance is reviewed, and forward-looking projections are created. Generally speaking, given the Company's typical loan and investment profile, a risk rating of three suggests that the Company expects the loan to make both principal and interest payments according to the contractual terms of the loan agreement, and is not considered impaired. A risk rating of four indicates the Company anticipates that the loan will require a modification of some kind. A risk rating of five indicates the Company expects the loan to underperform over its term, and that there could be loss of interest and/or principal. Ratings of 3.5 and 4.5 generally indicate loans that have characteristics of both the immediately higher and lower classifications. Further, while the above are the primary guidelines used in determining a certain risk rating, subjective items such as borrower strength, condition of the market of the underlying collateral, additional collateral or other credit enhancements, or loan terms, may result in a rating that is higher or lower

than might be indicated by any risk rating matrix.

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A summary of the loan portfolio's weighted average internal risk ratings and LTV ratios by asset class as of June 30, 2011 and December 31, 2010 is as follows:

Asset Class	Unpaid Principal Balance	As of June 30, 2011			
		Percentage of Portfolio	Wtd. Avg. Internal Risk Rating	First Dollar LTV Ratio	Last Dollar LTV Ratio
Multi-family	\$ 613,839,931	40.5%	3.6	22%	87%
Office	533,681,601	35.2%	3.2	44%	85%
Hotel	136,062,453	9.0%	3.8	44%	92%
Land	161,513,780	10.7%	4.1	0%	92%
Commercial	54,412,874	3.6%	3.6	0%	90%
Condo	14,650,000	1.0%	3.9	67%	91%
Total	\$ 1,514,160,639	100.0%	3.5	29%	87%

Asset Class	Unpaid Principal Balance	As of December 31, 2010			
		Percentage of Portfolio	Wtd. Avg. Internal Risk Rating	First Dollar LTV Ratio	Last Dollar LTV Ratio
Multi-family	\$ 615,788,256	37.7%	3.6	26%	87%
Office	563,914,007	34.5%	3.3	47%	87%
Hotel	220,277,021	13.5%	3.9	25%	95%
Land	164,161,755	10.0%	4.1	0%	94%
Commercial	55,073,229	3.4%	3.6	0%	92%
Condo	14,650,000	0.9%	3.9	66%	90%
Total	\$ 1,633,864,268	100.0%	3.6	30%	89%

Geographic Concentration Risk

As of June 30, 2011, 41%, 16%, and 7% of the outstanding balance of the Company's loans and investments portfolio had underlying properties in New York, California, and Florida, respectively. As of December 31, 2010, 38%, 15%, and 12% of the outstanding balance of the Company's loans and investments portfolio had underlying properties in New York, California and Florida, respectively.

Impaired Loans and Allowance for Loan Losses

The Company performs evaluations of the loan portfolio quarterly to assess the performance of its loans and whether a reserve for impairment should be recorded. The Company considers a loan impaired when, based upon current information and events, it is probable that it will be unable to collect all amounts due for both principal and interest according to the contractual terms of the loan agreement.

During the three months ended June 30, 2011, the Company determined that the fair value of the underlying collateral securing three impaired loans with an aggregate carrying value of \$50.5 million was less than the net carrying value of the loans, resulting in an \$11.4 million provision for loan losses. During the six months ended June 30, 2011, the Company determined that the fair value of the underlying collateral securing six impaired loans with an aggregate carrying value of \$72.3 million was less than the net carrying value of the loans, resulting in a \$12.9 million provision for loan losses. In addition, during the second quarter of 2011, the Company recorded net recoveries of \$3.8 million related to five loans in the Company's portfolio. During the first quarter of 2011, the Company recorded recoveries of \$1.0 million related to two loans in the Company's portfolio. These recoveries were recorded in provision for loan losses on the Consolidated Statement of Operations. The effect of the recoveries resulted in a provision for loan losses, net of recoveries, of \$7.6 million and \$8.1 million for the three and six months ended June 30, 2011, respectively. The \$11.4 million and \$12.9 million of loan loss reserves recorded during the three and six months ended June 30, 2011 was attributable to loans on which the Company had previously recorded reserves. The Company recorded a \$25.6 million and \$50.6 million provision for loan losses for the three and six months ended June 30, 2010, respectively, when it performed an evaluation of its loan portfolio and determined that the fair value of the underlying collateral securing 12 and 17 impaired loans, respectively, with

Table of Contents**ARBOR REALTY TRUST, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****June 30, 2011****(Unaudited)**

an aggregate carrying value of \$284.2 million and \$398.3 million, respectively, were less than the net carrying value of the loans. In addition, the Company also recorded a recovery of \$0.8 million received in the second quarter of 2010 for a fully reserved loan, the effect of which resulted in a provision for loan losses, net of recoveries, of \$24.8 million and \$49.8 million for the three and six months ended June 30, 2010, respectively. There were no loans for which the value of the collateral securing the loan was less than the carrying value of the loan for which the Company had not recorded a provision for loan loss.

At June 30, 2011, the Company had a total of 26 loans with an aggregate carrying value, before reserves, of \$318.9 million for which impairment reserves have been recorded. At December 31, 2010, the Company had a total of 30 loans with an aggregate carrying value, before reserves, of \$530.6 million for which impairment reserves have been recorded.

A summary of the changes in the allowance for loan losses is as follows:

	For the Six Months Ended June 30, 2011	For the Six Months Ended June 30, 2010
Allowance at beginning of the period	\$ 205,470,302	\$ 326,328,039
Provision for loan losses	12,900,000	50,580,000
Charge-offs	(10,724,862)	(40,780,256)
Charge-offs on loans reclassified to real estate owned, net	(31,710,929)	(5,600,000)
Recoveries of reserves	(4,703,146)	
Allowance at end of the period	\$ 171,231,365	\$ 330,527,783

A summary of charge-offs and recoveries is as follows:

	For the Six Months Ended	
	June 30, 2011	June 30, 2010
<i>Charge-offs:</i>		
Multi-family	\$ (21,971,114)	\$ (5,600,000)
Office	(7,114,677)	
Hotel	(13,350,000)	
Land		(35,350,926)
Condo		(5,429,330)
Total	\$ (42,435,791)	\$ (46,380,256)

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Recoveries:

Multi-family	\$	(821,389)	\$
Office		(3,881,757)	
Total	\$	(4,703,146)	\$

Net Charge-offs	\$	(37,732,645)	\$	(46,380,256)
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Ratio of net charge-offs during the period
to average loans and investments
outstanding during the period

2.4% 2.4%

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ARBOR REALTY TRUST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2011

(Unaudited)

A summary of the Company's impaired loans by asset class is as follows:

Asset Class	June 30, 2011			Three Months Ended June 30, 2011		Six Months Ended June 30, 2011	
	Unpaid Principal Balance	Carrying Value (1)	Allowance for Loan Losses	Average Recorded Investment (2)	Interest Income Recognized	Average Recorded Investment (2)	Interest Income Recognized
Multi-family	\$ 114,623,249	\$ 114,573,683	\$ 57,789,180	\$ 122,437,326	\$ 381,302	\$ 152,597,720	\$ 1,287,009
Office	34,219,603	29,145,388	17,000,000	59,219,128	506,554	62,712,473	1,599,669
Hotel	33,671,507	35,771,507	28,671,515	33,671,507	242,422	76,171,507	486,209
Land	130,255,660	129,378,936	58,700,000	130,255,660	8,622	130,255,661	16,978
Condo	10,000,000	10,000,000	9,070,670	10,000,000	77,125	10,000,000	137,125
Total	\$ 322,770,019	\$ 318,869,514	\$ 171,231,365	\$ 355,583,621	\$ 1,216,025	\$ 431,737,361	\$ 3,526,990

Asset Class	As of December 31, 2010			Three Months Ended June 30, 2010		Six Months Ended June 30, 2010	
	Unpaid Principal Balance	Carrying Value (1)	Allowance for Loan Losses	Average Recorded Investment (2)	Interest Income Recognized	Average Recorded Investment (2)	Interest Income Recognized
Multi-family	\$ 190,572,190	\$ 189,163,526	\$ 77,681,683	\$ 274,603,262	\$ 2,002,365	\$ 269,553,399	\$ 4,440,468
Office	91,205,342	86,132,382	27,996,434	41,540,342			