

IPARTY CORP  
Form 10-Q  
May 09, 2012

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

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FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Quarterly Period Ended March 31, 2012

OR

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Transition Period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-15611

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iPARTY CORP.  
(Exact Name of Registrant as Specified in Its Charter)

Delaware  
(State or Other Jurisdiction of  
Incorporation or Organization)

76-0547750  
(I.R.S. Employer  
Identification No.)

270 Bridge Street, Suite 301,  
Dedham, Massachusetts  
(Address of Principal Executive Offices)

02026  
(Zip Code)

(781) 329-3952  
(Registrant's Telephone Number, Including Area Code)

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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

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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 definition 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 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

As of May 3, 2012, there were 24,418,284 shares of common stock, \$.001 par value, outstanding.

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iPARTY CORP.  
QUARTERLY REPORT ON FORM 10-Q  
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## PART I - FINANCIAL INFORMATION

## Item 1. Financial Statements

iPARTY CORP.  
CONSOLIDATED BALANCE SHEETS  
(unaudited)

	Mar 31, 2012	Dec 31, 2011
<b>ASSETS</b>		
Current assets:		
Cash	\$62,450	\$63,650
Restricted cash	523,635	819,604
Accounts receivable	707,089	1,377,234
Inventories	16,612,714	15,965,507
Prepaid expenses and other assets	1,510,572	1,415,780
Deferred income tax asset	46,762	46,762
Total current assets	19,463,222	19,688,537
Property and equipment, net	2,603,817	2,664,086
Intangible assets, net	546,765	626,900
Other assets	311,068	333,731
Deferred income tax asset	540,841	540,841
Total assets	\$23,465,713	\$23,854,095
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable and book overdrafts	\$6,707,479	\$5,970,015
Accrued expenses	2,133,309	2,295,467
Current portion of capital lease obligations	2,307	4,613
Borrowings under line of credit	5,577,293	5,366,512
Total current liabilities	14,420,388	13,636,607
Long-term liabilities:		
Deferred rent	1,519,158	1,504,973
Commitments and contingencies		
Stockholders' equity:		
Convertible preferred stock - \$.001 par value; 10,000,000 shares authorized,		
Series B convertible preferred stock - 1,150,000 shares authorized; 420,408 shares issued and outstanding (aggregate liquidation value of \$8,408,160 at March 31, 2012)	6,255,671	6,255,671
Series C convertible preferred stock - 100,000 shares authorized, issued and outstanding (aggregate liquidation value of \$2,000,000 at March 31, 2012)	1,492,000	1,492,000
Series D convertible preferred stock - 250,000 shares authorized, issued and outstanding (aggregate liquidation value of \$5,000,000 at March 31, 2012)	3,652,500	3,652,500
Series E convertible preferred stock - 533,333 shares authorized; 296,666 shares issued and outstanding (aggregate liquidation value of \$1,112,497 at March 31, 2012)	1,112,497	1,112,497
Series F convertible preferred stock - 114,286 shares authorized, issued and outstanding (aggregate liquidation value of \$500,000 at March 31, 2012)	500,000	500,000
Total convertible preferred stock	13,012,668	13,012,668

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Common stock - \$.001 par value; 150,000,000 shares authorized; 24,408,594 shares issued and outstanding	24,409	24,409
Additional paid-in capital	53,036,492	52,987,574
Accumulated deficit	(58,547,402)	(57,312,136)
Total stockholders' equity	7,526,167	8,712,515
Total liabilities and stockholders' equity	\$23,465,713	\$23,854,095

The accompanying notes are an integral part of these Consolidated Financial Statements.

iPARTY CORP.  
CONSOLIDATED STATEMENTS OF OPERATIONS  
(unaudited)

	For the three months ended	
	Mar 31, 2012	Mar 26, 2011
Revenues	\$ 15,753,745	\$ 15,092,128
Operating costs:		
Cost of products sold and occupancy costs	10,026,180	9,600,871
Marketing and sales	5,210,909	5,136,742
General and administrative	1,702,376	1,786,022
Operating loss	(1,185,720 )	(1,431,507 )
Change in fair value of warrant liability	(216 )	(6,222 )
Interest income	-	23
Interest expense	(49,330 )	(73,205 )
Loss before income taxes	(1,235,266 )	(1,510,911 )
Income taxes	-	-
Net loss	\$(1,235,266 )	\$(1,510,911 )
Loss per share:		
Basic and diluted	\$(0.05 )	\$(0.06 )
Weighted-average shares outstanding:		
Basic and diluted	24,408,594	24,319,464

The accompanying notes are an integral part of these Consolidated Financial Statements.

iPARTY CORP.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(unaudited)

	For the three months ended	
	Mar 31, 2012	Mar 26, 2011
Operating activities:		
Net loss	\$(1,235,266)	\$(1,510,911)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	272,065	296,080
Amortization	89,531	100,518
Deferred rent	14,185	(8,720 )
Non-cash stock-based compensation expense	48,702	44,672
Change in fair value of warrants	216	6,222
Changes in operating assets and liabilities:		
Accounts receivable	670,145	(39,288 )
Inventories	(647,207 )	(900,043 )
Prepaid expenses and other assets	(81,525 )	2,411
Accounts payable and book overdrafts	737,465	1,029,444
Accrued expenses and other liabilities	(162,158 )	(399,561 )
Net cash used in operating activities	(293,847 )	(1,379,176)
Investing activity:		
Purchase of property and equipment	(211,796 )	(300,653 )
Net cash used in investing activity	(211,796 )	(300,653 )
Financing activities:		
Net borrowings under line of credit	210,781	1,482,504
Decrease in restricted cash	295,969	176,529
Principal payments on capital lease obligations	(2,307 )	(2,307 )
Proceeds from exercise of stock options	-	24,103
Net cash provided by financing activities	504,443	1,680,829
Net (decrease) increase in cash	(1,200 )	1,000
Cash beginning of period	63,650	62,650
Cash end of period	\$62,450	\$63,650
Supplemental disclosure of non-cash financing activities:		
Disposal of property and equipment	\$8,258	\$-

The accompanying notes are an integral part of these Consolidated Financial Statements.





iPARTY CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2012

(unaudited)

1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES:

Interim Financial Information

The interim consolidated financial statements as of March 31, 2012 have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC") for interim financial reporting. These consolidated statements are unaudited and, in the opinion of management, include all adjustments (consisting of normal recurring adjustments and accruals) necessary to present fairly the consolidated balance sheets, consolidated operating results, and consolidated cash flows for the periods presented in accordance with U.S. generally accepted accounting principles. The consolidated balance sheet at December 31, 2011 has been derived from the audited consolidated financial statements at that date. Operating results for the Company on a quarterly basis may not be indicative of the results for the entire year due, in part, to the seasonality of the party goods industry. Historically, higher revenues and operating income have been experienced in the second and fourth fiscal quarters, while the Company has generated losses in the first and third quarters. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been omitted in accordance with the rules and regulations of the SEC. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements, and accompanying notes, included in the Company's Annual Report on Form 10-K, for the year ended December 31, 2011.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary after elimination of all significant intercompany transactions and balances.

Revenue Recognition

Revenues include the selling price of party goods sold, net of returns and discounts, and are recognized at the point of sale. The Company estimates returns based upon historical return rates and such amounts have not been significant to date.

Concentrations

The Company purchases its inventory from a diverse group of vendors. Five suppliers accounted for approximately 48.5% of the Company's purchases of merchandise for the three months ended March 31, 2012, but the Company does not believe that it is overly dependent upon any single source for its merchandise, often using more than one vendor for similar kinds of products.

The Company entered into a Supply Agreement with its largest supplier, Amscan, Inc. ("Amscan") on August 7, 2006. Beginning with calendar year 2008, the Supply Agreement requires the Company to purchase on an annual basis merchandise equal to the total number of stores open, excluding temporary stores, during such calendar year, multiplied by \$180,000. The Supply Agreement provides for penalties in the event the Company fails to attain the annual purchase commitment that would require the Company to pay the difference between the purchases for that year and the annual purchase commitment for that year. Under the terms of the Supply Agreement, the annual purchase commitment for any individual year can be reduced for orders placed by the Company but not filled within a

specified time period by the supplier. The Company's purchases for 2009 fell short of the required annual commitment by approximately \$368,000. The supplier agreed to allow the Company to roll over any shortfall for the year 2009 into future years' requirements. The Company's purchases in 2010 exceeded the minimum purchase requirements for that year in addition to the 2009 shortfall. The Company's purchases in 2011 exceeded the minimum purchase requirements for that year. The Company is not aware of any reason that would prevent it from meeting the minimum purchase requirements during the remaining term of the Supply Agreement,

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On December 30, 2010, the Company and Amscan agreed to extend the original expiration of the Supply Agreement from the original expiration date of December 31, 2012 to December 31, 2013. In addition, on December 30, 2010, the Company agreed with Party City Corporation (“Party City”), an affiliate of Amscan, to take over one Party City leased location in Manchester, Connecticut on March 1, 2011. As part of the store takeover, the Company entered into an amendment to that certain Asset Purchase Agreement dated August 7, 2006 with Party City to extend the term of the non-compete provisions with Party City and its affiliates contained in the Asset Purchase Agreement from August 7, 2011 until December 31, 2013 and to include the Manchester, Connecticut location as part of the restricted area in the non-compete provisions.

#### Accounts Receivable

Accounts receivable primarily represent amounts due from credit card companies and from vendors for inventory rebates. Management does not provide for doubtful accounts as such amounts have not been significant to date; the Company does not require collateral.

#### Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

#### Cash and Restricted Cash

The Company uses controlled disbursement banking arrangements as part of its cash management program. Outstanding checks, which were included in accounts payable and book overdrafts, totaled \$1,998,401 at March 31, 2012 and \$2,000,025 at December 31, 2011.

Restricted cash represents funds on deposit established for the benefit of and under the control of Wells Fargo Bank, National Association (successor by merger to Wells Fargo Retail Finance, LLC) (“Wells Fargo”), the Company’s lender under its line of credit, and constitutes collateral for amounts outstanding under this line.

#### Fair Value of Financial Instruments

The carrying values of cash and cash equivalents, accounts receivable and accounts payable approximate fair value because of the short-term nature of these instruments. The fair value of borrowings under the Company’s line of credit approximates the carrying value because the debt bears interest at a variable market rate. The fair value of the capital lease obligations approximates the carrying value. The fair value at March 31, 2012 of the warrants issued in 2008 was determined by using the Black-Scholes model (implied volatility of 104.7%, risk free rate of 0.19% and expected life of 0.91 years).

#### Inventories

Inventories consist of party supplies and are valued at the lower of moving weighted-average cost or market which approximates FIFO (first-in, first-out). The Company records vendor rebates, discounts and certain other adjustments to inventories, including freight costs, and these amounts are recognized in the income statement as the related goods are sold.

Net Loss per Share

Net loss per basic share is computed by dividing net loss available to common shareholders by the weighted-average number of common shares outstanding. The common share equivalents of Series B-F preferred stock are required to be included in the calculation of net loss per basic share in accordance with Accounting Standards Codification (ASC) 260-10-45, Earnings Per Share – Other Presentation Matters. Since the preferred stockholders are entitled to participate in dividends when and if declared by the Board of Directors on the same basis as if the shares of Series B-F preferred stock were converted to common stock, the application of ASC 260-10-45 has no effect on the amount of net income per basic share of common stock. For periods with net losses, the Company does not allocate losses to Series B-F preferred stock.

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Net income (loss) per diluted share under ASC 260-10-45 is computed by dividing net income (loss) by the weighted-average number of common shares outstanding plus, if dilutive, the common share equivalents of Series B-F preferred stock on an as if-converted basis, plus the common share equivalents of the “in the money” stock options and warrants as computed by the treasury method. For the periods with net losses, the Company excludes those common share equivalents since their impact would be anti-dilutive.

The following table sets forth the computation of net loss per basic and diluted share available to common stockholders:

	For the three months ended	
	Mar 31, 2012	Mar 26, 2011
Common shares	\$ (1,235,266 )	\$ (1,510,911 )
Convertible preferred Series B-F	-	-
Net loss	\$ (1,235,266 )	\$ (1,510,911 )
Net loss per share		
Basic and diluted	\$ (0.05 )	\$ (0.06 )
Weighted-average shares outstanding:		
Common shares - basic	24,408,594	24,319,464
Common share equivalents of Series B-F convertible preferred stock	-	-
If - converted weighted-average shares outstanding	24,408,594	24,319,464

The common stock equivalents of Series B-F preferred stock calculated on an if converted basis totaled 14,521,687 and 14,918,052 shares for the three months ended March 31, 2012 and March 26, 2011, respectively. These share amounts have been excluded from net loss per share since their impact would have been anti-dilutive.

The common share equivalents of “out of the money” stock options and warrants which were also excluded from the computation of net loss per diluted share available to common stockholders were 6,135,964 and 100,000 in the first quarter of 2012, and 4,787,150 and 2,183,334 in the first quarter of 2011, respectively.

#### Stock-Based Compensation Expense

The Company uses the Black-Scholes option pricing model to determine the fair value of stock-based compensation. The Black-Scholes model requires the Company to make several subjective assumptions, including the estimated length of time employees will retain their vested stock options before exercising them (“expected term”), and the estimated volatility of the Company’s common stock price over the expected term, which is based on historical volatility of the Company’s common stock over a time period equal to the expected term. The Black-Scholes model also requires a risk-free interest rate, which is based on the U.S. Treasury yield curve in effect at the time of the grant, and the dividend yield on the Company’s common stock, which is assumed to be zero since the Company does not pay dividends and has no current plans to do so in the future. Changes in these assumptions can materially affect the estimate of fair value of stock-based compensation and consequently, the related expense recognized in the consolidated statements of operations. The Company recognizes stock-based compensation expense on a straight-line basis over the vesting period of each grant.

The stock-based compensation expense recognized by the Company was:

	For the three months ended	
	Mar 31, 2012	Mar 26, 2011
Stock-based compensation expense	\$ 48,702	\$ 44,672

Stock-based compensation expense is included in general and administrative expense and had no impact on cash flow from operations and cash flow from financing activities for the three months ended March 31, 2012 or March 26, 2011.

On May 27, 2009, the Company's stockholders approved a new equity incentive plan entitled the 2009 Stock Incentive Plan (the "2009 Plan"). The Company no longer grants equity awards under its former equity incentive plan, the Amended and Restated 1998 Incentive and Nonqualified Stock Option Plan (the "1998 Plan" and with the 2009 Plan, the "Plans").

Under the Company's Plans, options to acquire shares of common stock may be granted to officers, directors, key employees and consultants. Under the 2009 Plan, the exercise price for qualified incentive options and non-qualified options cannot be less than the fair market value of the stock on the grant date, as determined by the Company's Board of Directors. In addition, under the 2009 Plan, other stock-based and performance awards may be granted to officers, directors, key employees and consultants, including stock appreciation rights, restricted stock, and restricted stock units. Under the Plans, a combined total of 11,000,000 shares of common stock or other stock based awards may be granted. To date, the Company has only issued options for shares under its Plans, which have been granted to employees, directors and consultants of the Company at fair market value at the date of grant. Of the options that have been issued, options for 1,548,751 shares have been exercised and options for 8,033,794 shares remain outstanding at March 31, 2012. Generally, employee options become exercisable over periods of up to four years, and expire ten years from the date of grant.

At the annual Board of Directors meetings following the Company's annual stockholders meetings, the Company granted options to its key employees, including its CEO and CFO, and independent directors as follows: (i) 817,100 options for the purchase of shares of common stock on June 10, 2011 at an exercise price of \$0.28 per share, and (ii) 502,320 options for the purchase of shares of common stock on June 2, 2010 at an exercise price of \$0.30 per share. Also, the Company granted options for the purchase of an aggregate of (i) 633,400 options for the purchase of shares of common stock to key employees on January 18, 2012 at an exercise price of \$0.14 per share and (ii) 165,000 shares of common stock to key employees on March 11, 2010 at an exercise price of \$0.41 per share. The fair value using the Black-Scholes option pricing model of the options granted on January 18, 2012 was \$0.12 per share, \$0.23 per share for the options granted on June 10, 2011, \$0.25 per share for the options granted on June 2, 2010, and \$0.34 per share for the options granted on March 11, 2010. The exercise prices for each of the option grants made in 2010, 2011 and 2012 was equal to the grant date closing price of the Company's common stock as reported on the NYSE Amex.

On April 1, 2010, in accordance with the related provisions of new employment contracts executed as of that date, options to purchase 720,000 shares of common stock granted on May 27, 2009 to the Company's Chief Executive Officer and Senior Vice President – Merchandising and Marketing were accelerated and became fully vested. The acceleration of the options resulted in immediate recognition of expense in the amount of \$48,204. In addition, on July 1, 2010, the Company granted options for the purchase of 675,000 shares of common stock to these two executives, pursuant to their new employment contracts, at an exercise price of \$0.27 per share. One third of each of these executives' options vested on July 1, 2010, the grant date, with the remaining options vesting as to one third on each of the next two grant date anniversaries. The fair value using the Black-Scholes option pricing model of the July 1, 2010 executive options was \$0.22 per share.



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The weighted average fair value of the options at the date of the grant for options granted during the three months ended March 31, 2012 and March 26, 2011 was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions:

	For the three months ended Mar 31, 2012
Risk-free interest rate	0.82%
Expected volatility	112.90%
Weighted average expected life (in years)	6.87
Expected dividends	0.00%

There were no options granted during the three months ended March 26, 2011.

A summary of the Company's stock options is as follows:

	Number of Stock Options	Weighted Average Exercise Price	Price Range	Average Remaining Life (Years)	Aggregate Intrinsic Value
Outstanding - December 31, 2011	7,542,459	0.41	0.07 - 1.33		
Granted	633,400	0.14	0.14 - 0.14		
Expired/forfeited	(142,065 )	0.36	0.30 - 0.39		
Exercised	-	-	- - -		
Outstanding - March 31, 2012	8,033,794	0.39	0.07 - 1.33	5.70	121,886
Exercisable - March 31, 2012	6,318,960	0.44	0.07 - 1.33	4.90	87,456
Available for grant - March 31, 2012	1,417,455				

The following table summarizes information for options outstanding and exercisable at March 31, 2012:

Price Range	Number of Stock Options	Outstanding	Weighted Average Exercise Price	Exercisable	
		Weighted Average Remaining Life (Years)		Number of Stock Options	Weighted Average Exercise Price
\$ 0.07 - \$ 0.20	1,918,760	7.9	\$ 0.12	1,199,082	\$ 0.11
0.21 - 0.30	2,182,725	8.3	0.28	1,270,099	0.28
0.31 - 0.50	2,130,401	4.0	0.39	2,047,871	0.39
0.51 - 1.00	1,764,908	2.3	0.81	1,764,908	0.81
1.01 - 1.33	37,000	1.6	1.12	37,000	1.12
Total	8,033,794	5.7	\$ 0.39	6,318,960	\$ 0.44

The remaining unrecognized stock-based compensation expense related to unvested awards at March 31, 2012 was \$278,852 and the period of time over which this expense will be recognized is 2.8 years.





## Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and are depreciated on the straight-line method over the estimated useful lives of the assets. Expenditures for maintenance and repairs are charged to operations as incurred. A listing of the estimated useful life of the various categories of property and equipment is as follows:

Asset Classification	Estimated Useful Life
Leasehold improvements	Lesser of term of lease or 10 years
Furniture and fixtures	7 years
Computer hardware and software	3 years
Equipment	5 years

## Intangible Assets

Intangible assets consist primarily of (i) the values of two non-compete agreements acquired in conjunction with the purchase of retail stores in 2006 and 2008, and (ii) the values of retail store leases acquired in those transactions. These assets have been accounted for at fair value as of their respective acquisition dates using significant other observable inputs, or Level 2 criteria, defined in the Fair Value Measurements section below.

The first non-compete agreement, from Party City and its affiliates, originally covered Massachusetts, Maine, New Hampshire, Vermont, Rhode Island, and Windsor and New London counties in Connecticut, and was to expire in 2011. This non-compete agreement had an original estimated life of 60 months. On December 30, 2010, the Company executed an agreement with Party City to take over its leased location in Manchester, Connecticut. Under that agreement, the term of the earlier non-compete agreement was extended to December 31, 2013 and the non-compete area was amended to include a three mile radius around the Manchester, Connecticut store. The other non-compete agreement was acquired in connection with the Company's purchase in January 2008 of the two party supply stores in Lincoln and Warwick, Rhode Island described above. This non-compete agreement covers Rhode Island for five years from the date of closing and within a certain distance from the Company's stores in the rest of New England for three years. The New England non-compete under this agreement has expired. The second non-compete agreement has an estimated life of 60 months. Both non-compete agreements are subject to certain terms and conditions in their respective acquisition agreements.

The occupancy valuations relate to acquired retail store leases for stores in Peabody, Massachusetts (estimated life of 90 months), Lincoln, Rhode Island (estimated life of 79 months) and Warwick, Rhode Island (estimated life of 96 months).

Intangible assets as of March 31, 2012 and December 31, 2011 were:

	March 31, 2012	December 31, 2011
Non-compete agreements	\$ 2,358,540	\$ 2,358,540
Occupancy valuations	944,716	944,716
Other	157,855	157,855
<b>Intangible assets</b>	<b>3,461,111</b>	<b>3,461,111</b>
<b>Less: accumulated amortization</b>	<b>(2,914,346 )</b>	<b>(2,834,211 )</b>

Intangible assets, net	\$ 546,765	\$ 626,900
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Amortization expense for these intangible assets was:

	For the three months ended	
	Mar 31, 2012	Mar 26, 2011
Amortization expense	\$ 80,135	\$ 79,203

Non-compete agreements are amortized based on the pattern of their expected cash flow benefits over the terms of the agreements. As a consequence of the December 30, 2010 amendment of the Party City non-compete agreement, the remaining unamortized asset associated with that agreement is being amortized over its remaining term, as amended. Occupancy valuations are amortized on a straight line basis over the terms of the related leases ranging from 79 to 96 months. The non-compete agreement amortization expense is included in general and administrative expense on the Consolidated Statements of Operations. The occupancy valuation amortization expense is included in cost of products sold and occupancy costs.

Future amortization expense related to these intangible assets as of March 31, 2012 is:

Year	Amount
2012	\$ 240,406
2013	208,761
2014	59,848
2015	37,750
Total	\$ 546,765

#### Accounting for the Impairment of Long-Lived Assets

The Company reviews each store for impairment indicators whenever events and changes in circumstances suggest that the carrying amounts may not be recoverable from estimated future store cash flows. The Company's review considers store operating results, future sales growth and cash flows. During the fourth quarter of the Company's fiscal year ended December 31, 2011, the Company determined that one of its retail stores was impaired due to underperforming sales. As a result of this impairment, a charge of approximately \$26,000 was recorded to reduce to fair value (\$0) the remaining carrying value of the property and equipment utilized in this store. The Company is not aware of any impairment indicators for any of our other stores at March 31, 2012.

#### Line of Credit

On October 14, 2011, the Company and its wholly owned subsidiary, as borrowers, entered into the First Amendment (the "Amendment") to the Second Amended and Restated Credit Agreement by and among the Company, its wholly owned subsidiary, and Wells Fargo Bank, National Association, as administrative agent and collateral agent, (the "Facility"). The Amendment continues the Facility in the amount of up to \$12,500,000 and extends the maturity date of the Facility to October 14, 2016. The Facility also allows the Company to increase the Facility up to a maximum level of \$15,000,000. The amount of credit that is available from time to time under the Facility continues to be determined as a percentage of the value of eligible inventory plus a percentage of the value of eligible credit card receivables, reduced by certain reserve amounts that may be required by Wells Fargo.

The Facility, as amended, provides for interest of 0.25% above Wells Fargo's base rate, or, at the Company's election, 2.00% above the London Interbank Offered Rate ("LIBOR"). The Facility also provides for letters of credit for up to a sublimit of \$2 million to be used in connection with inventory purchases. The obligations of the Company under the Facility are secured by a lien on substantially all its personal property.

The Facility contains a number of restrictive covenants, such as incurrence, payment or entry into certain indebtedness, liens, investments, acquisitions, mergers, dispositions and dividends. The Facility contains events of default customary for credit facilities of this type. Upon an event of default that is not cured or waived within any applicable cure periods, in addition to other remedies that may be available to Wells Fargo, the obligations under the Facility may be accelerated, outstanding letters of credit may be required to be cash collateralized and Wells Fargo may exercise remedies to collect the balance due, including to foreclose on the collateral.

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The Facility includes a financial covenant requiring the Company to maintain a minimum availability under the line of 7.5% of the credit limit, except for the period from January 1, 2012 through April 30, 2012, during which period the minimum availability is zero. At the current credit limit of \$12,500,000, the minimum availability will be \$937,500 when the 7.5% limit is restored on May 1, 2012. The Facility also has a covenant that requires the Company to limit its capital expenditures to within 110% of those amounts included in its business plan, which may be updated from time to time. As of March 31, 2012 and as of December 31, 2011, the Company was in compliance with all debt covenants. The Agreement also includes a 0.375% unused line fee. The line generally prohibits the payment of any dividends or other distributions to any of the Company's classes of capital stock.

The amounts outstanding under the Facility as of March 31, 2012 and December 31, 2011 were \$5,577,293 and \$5,366,512, respectively. The interest rate on these borrowings was 3.0% at March 31, 2012 and 2.8% at December 31, 2011. The outstanding balances under the Facility are classified as current liabilities in the accompanying consolidated balance sheets since the Company is required to apply daily lock box receipts to reduce the amount outstanding. At March 31, 2012, the Company had \$4,509,213 of additional availability under the Facility.

#### Stockholders' Equity

Upon the expiration of the Highbridge Warrant on September 15, 2011, the conversion prices of the Series B, C, and D convertible preferred stock were recomputed to reflect the reversal of the anti-dilution adjustment calculated at the warrant's issuance in 2006. As a result, the outstanding shares of these three series of preferred stock are now convertible into approximately 385,514 fewer shares of common stock. The expiration of the Highbridge Warrant had no impact on the Series E or F convertible preferred stock or any of the other outstanding warrants.

#### Fair Value Measurements

The Company follows the provisions of ASC 820, Fair Value Measurements and Disclosures. ASC 820 defines fair value as the price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. ASC 820 also describes three levels of inputs that may be used to measure the fair value:

Level 1 – quoted prices in active markets for identical assets or liabilities

Level 2 – observable inputs other than quoted prices in active markets for identical assets or liabilities

Level 3 – unobservable inputs in which there is little or no market data available, which require the reporting entity to develop its own assumptions

The only assets and liabilities subject to fair value measurement standards at March 31, 2012 and December 31, 2011 are cash and restricted cash which are based on Level 1 inputs, the warrant liability which is based on Level 2 inputs and certain impaired assets at one of the Company's retail stores which are based on Level 3 inputs.

## Income taxes

The Company has not provided for income taxes for the first quarter of fiscal 2012 or fiscal 2011 due to the availability of net operating loss (NOL) carryforwards to eliminate federal taxable income on an annual basis, and uncertainty of state taxable income based on the extent of our operating loss through March 31, 2012. No benefit has been recognized with respect to current losses or NOL carryforwards in these periods due to the uncertainty of future taxable income beyond 2012, the assessment of which depends largely on our operating results during our fourth quarter. We continue to believe we will be able to realize the deferred tax asset of \$587,603 based on estimated 2012 taxable income.

At the end of 2011, the Company had estimated net operating loss carryforwards of approximately \$16.6 million, which begin to expire in 2020. In accordance with Section 382 of the Internal Revenue Code, the use of these carryforwards may be subject to annual limitations based upon certain ownership changes of the Company's stock that may have occurred or that may occur.

## 2. SUBSEQUENT EVENTS

The Company has evaluated subsequent events as required by ASC 855, Subsequent Events, and has determined that there were no subsequent events requiring disclosure in these interim consolidated financial statements.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the unaudited Consolidated Financial Statements and related Notes included in Item 1 of this Quarterly Report on Form 10-Q and the audited Consolidated Financial Statements and related Notes and Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations", contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

Certain statements in this Quarterly Report on Form 10-Q, particularly statements contained in this Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations" constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The words "anticipate", "believe", "estimate", "expect", "plan", "intend" and similar expressions are intended to identify these forward-looking statements, but are not the exclusive means of identifying them. Forward-looking statements included in this Quarterly Report on Form 10-Q or hereafter included in our other publicly available documents filed with the Securities and Exchange Commission ("SEC"), reports to our stockholders and other publicly available statements issued or released by us involve known and unknown risks, uncertainties, and other factors which could cause our actual results, performance (financial or operating) or achievements to differ from the future results, performance (financial or operating) or achievements expressed or implied by such forward looking statements. Such future results are based upon our best estimates based upon current conditions and the most recent results of operations. Various risks, uncertainties and contingencies could cause our actual results, performance or achievements to differ materially from those expressed in, or implied by, the forward-looking statements contained in this Quarterly Report on Form 10-Q. These include, but are not limited to, those described below under the heading "Factors That May Affect Future Results" and in our most recently filed Annual Report on Form 10-K for the fiscal year ended December 31, 2011 and our other periodic reports filed with the SEC. We assume no obligation to update these forward looking statements contained in this report, whether as a result of new information, future events or otherwise.

### Overview

We are a party goods retailer operating stores throughout New England, where 47 of our 52 retail stores are located, and in Florida in addition to an online e-commerce site. We believe we are a leading brand in the party industry in the retail markets we serve and a leading resource in those markets for consumers seeking party goods, party planning advice and information.

Our 52 retail stores are located predominantly in New England with 7 stores in Connecticut, 6 in New Hampshire, 3 in Rhode Island, 3 in Maine, 1 in Vermont, and 27 in Massachusetts. We also operate 5 stores in Florida. In July 2011, we re-launched our newly redesigned e-commerce site with a full assortment of costume and related merchandise for purchase and shipping via the internet. In the first quarter of 2012, we added kids' birthday, graduation and certain seasonal assortments to the e-commerce site. We plan to continue to expand our e-commerce offerings during the remainder of 2012. We also use our internet site to highlight the changing store product assortment and feature sales flyers, promotions and coupons to increase customer visits to our retail stores.

During the 2011 Halloween season, we operated eleven temporary stores, the same number of temporary stores operated during the 2010 Halloween season. In December 2010, we opened a new store in the South Bay Center, Boston, Massachusetts and entered into an agreement to take over an additional store from a competitor in Manchester, Connecticut in the first quarter of 2011, which opened in March 2011. In January 2012, we reopened our store in West Lebanon, New Hampshire, which had been closed due to flood damage since August 2011, and we closed our older store in Manchester, Connecticut.



Our stores range in size from approximately 7,000 square feet to 20,295 square feet and average approximately 10,299 square feet in size.

We lease our properties, typically for 10 years and usually with options from our landlords to renew our leases for an additional 5 or 10 years.

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The following table shows the number of stores in operation (not including temporary stores):

	For the three months ended	
	Mar 31, 2012	Mar 26, 2011
Beginning of period	52	52
Openings / Acquisitions	1	1
Closings	(1 )	-
End of period	52	53

Our stores feature over 20,000 products ranging from paper party goods, Halloween costumes, greeting cards and balloons to more unique merchandise such as piñatas, tiny toys, masquerade and Hawaiian luau items. Our sales are primarily driven by the following holiday and party events: Halloween, Christmas, Easter, Valentine's Day, New Year's, Independence Day, St. Patrick's Day, Thanksgiving, Chanukah and sports championships. We also focus our business closely on lifetime events such as anniversaries, graduations, birthdays, and bridal and baby showers.

#### Trends and Quarterly Summary

Our business has a seasonal pattern. In the past three years, we have realized an average of approximately 36.2% of our annual revenues in our fourth quarter, which includes Halloween and Christmas, and an average of approximately 24.6% of our revenues in the second quarter, which includes school graduations, and often the Easter holiday. Also, during these past three years, we have had net income in our second and fourth quarters and generated losses in our first and third quarters.

#### First Quarter Summary

For the first quarter of 2012, our consolidated revenues were \$15.8 million, compared to \$15.1 million for the first quarter of 2011. The increase in first quarter revenues from the year-ago period included an 8.6% increase in comparable store sales (sales from stores open more than one year). The increase in consolidated revenue was driven by higher comparable store sales in a number of areas, including the New England Patriots – New York Giants Super Bowl merchandise, a very strong performance in St. Patrick's Day seasonal merchandise, and by gains in some of our basic areas such as birthday, masquerade and wedding. In addition to our comparable store sales gains, we also saw improved sales in our Manchester, Connecticut market, where we replaced an older store with one acquired last year from a competitor. Consolidated gross profit margin was 36.4% for the first quarter of 2012, equal to the gross profit margin for the same period in 2011. The gross profit margin components included a decrease of 0.2% in product selling margin rate, offset by an equal improvement in occupancy rate as a result of improved leveraging of occupancy costs based on the increase in same store sales. The consolidated net loss for the first quarter of 2012 was \$1.2 million, or \$0.05 per share, compared to \$1.5 million, or \$0.06 per share, for the first quarter of 2011.

#### Acquisition and Growth Strategy

Our growth strategy for 2012 and beyond includes expanding and targeting the temporary Halloween store aspect of our business, opening new stores, relocating or consolidating existing stores, reviewing potential acquisition of other entities, and developing our e-commerce site. In March 2011, we took over a competitor's Manchester, Connecticut store. In addition, we opened eleven temporary Halloween stores in 2011. Any determination whether to open a new or temporary store or make an acquisition is based upon a variety of factors, including, without limitation, the purchase price and other financial terms of the transaction, our liquidity and ability to finance the transaction, the business prospects, geographical location and the extent to which any new or temporary store or acquisition would

enhance our business.

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## Results of Operations

Fiscal year 2012 has 52 weeks and ends on December 29, 2012. Fiscal year 2011 had 53 weeks and ended on December 31, 2011.

The first quarter of fiscal year 2012 had 13 weeks and ended on March 31, 2012. The first quarter of fiscal year 2011 had 13 weeks and ended on March 26, 2011.

## Three Months Ended March 31, 2012 Compared to Three Months Ended March 26, 2011

## Revenues

Revenues include the selling price of party goods sold, net of returns and discounts, and are recognized at the point of sale or at the time of shipment for internet sales. Our consolidated revenues for the first quarter of fiscal 2012 were \$15,753,745, an increase of \$661,617, or 4.4% from the first quarter of the prior fiscal year. The increase was primarily due to increased sales in our comparable stores of 8.6% in the first quarter of 2012 compared to the first quarter of 2011. The largest components of the increase in comparable store sales included approximately \$561,000 in the fall and bulk categories, \$122,000 in masquerade, and \$103,000 in St. Patrick's Day merchandise. The increase in fall and bulk sales came largely from sales related to the 2012 Super Bowl event.

	For the three months ended	
	Mar 31, 2012	Mar 26, 2011
Revenues	\$ 15,753,745	\$ 15,092,128
Increase (decrease) in revenues	4.4	% 1.7

The increase in comparable store sales was partly offset in the first quarter of 2012 by the shift in timing of the New Year's holiday in relation to our fiscal calendar, which was brought about by the addition of the 53rd fiscal week in fiscal year 2011, which resulted in very low New Year's merchandise sales in the first quarter of 2012 compared to the first quarter of 2011.

## Cost of products sold and occupancy costs

Cost of products sold and occupancy costs consist of the cost of merchandise sold to customers and the occupancy costs for our stores. Our cost of products sold and occupancy costs for the first quarter of fiscal 2012 were \$10,026,180 or 63.6% of revenues, an increase of \$425,309, and equal as a percentage of revenues, compared to the first quarter of the prior fiscal year.

	For the three months ended	
	Mar 31, 2012	Mar 26, 2011
Cost of products sold and occupancy costs	\$ 10,026,180	\$ 9,600,871
Percentage of revenues	63.6	% 63.6

As a percentage of revenues, cost of products sold and occupancy costs included a decrease in product selling margins of 0.2% offset by an equal decrease in occupancy costs as a percentage of revenues from improved leveraging of those costs based on increased sales in the first quarter of 2012 compared to the same period in 2011.



## Marketing and sales expense

Marketing and sales expense consists primarily of advertising and promotional expenditures, all store payroll and related expenses for personnel engaged in marketing and selling activities and other non-payroll expenses associated with operating our stores. Our consolidated marketing and sales expense for the first quarter of fiscal 2012 was \$5,210,909, or 33.1% of revenues, an increase of \$74,167 and a decrease of 0.9 percentage points, as a percentage of revenues, from the first quarter of the prior fiscal year. The increase in marketing and sales expense was primarily due to an increase in headquarters marketing payroll and advertising expenses, partly offset by a decrease in store payroll and depreciation costs in the first quarter of 2012 compared to the first quarter of 2011.

	For the three months ended			
	Mar 31, 2012		Mar 26, 2011	
Marketing and sales	\$	5,210,909	\$	5,136,742
Percentage of revenues		33.1	%	34.0
				%

As a percentage of revenues, the decrease in marketing and sales expense was primarily due to higher same store sales that increased leveraging of payroll expenses in the first quarter of 2012 compared to the first quarter of 2011.

## General and administrative expense

General and administrative (“G&A”) expense consists of payroll and related expenses for executive, merchandising, finance and administrative personnel, as well as information technology, professional fees and other general corporate expenses. Our consolidated G&A expense for the first quarter of fiscal 2012 was \$1,702,376 or 10.8% of revenues, a decrease of \$83,646 or 1.0 percentage points, as a percentage of revenues, from the first quarter of the prior fiscal year. The decrease in general and administrative expense was primarily due to lower professional fees in the first quarter of 2012 compared to the first quarter of 2011.

	For the three months ended			
	Mar 31, 2012		Mar 26, 2011	
General and administrative	\$	1,702,376	\$	1,786,022
Percentage of revenues		10.8	%	11.8
				%

The decrease in general and administrative expense as a percentage of revenues from the first quarter of the prior fiscal year was primarily due to the reduction in the dollar amount of those expenses, as discussed above, plus increased leveraging of general and administrative expense in the first quarter of 2012 compared to the first quarter of 2011 based on higher same store sales.

## Operating loss

Our operating loss for the first quarter of fiscal 2012 was \$1,185,720, or 7.5% of revenues, as compared to \$1,431,507, or 9.5% of revenues for the first quarter of the prior fiscal year.

## Interest expense

Our interest expense in the first quarter of fiscal 2012 was \$49,330, a decrease of \$23,875 from the first quarter of the prior fiscal year. The decrease in the first quarter of fiscal 2012 as compared to the prior period was primarily due to lower effective interest rates in the first quarter of 2012 compared to the same period in 2011.



## Income taxes

We have not provided for income taxes for the first quarter of fiscal 2012 or fiscal 2011 due to the availability of net operating loss (NOL) carryforwards to eliminate federal taxable income on an annual basis, and uncertainty of state taxable income based on the extent of our operating loss through March 31, 2012. No benefit has been recognized with respect to current losses or NOL carryforwards in these periods due to the uncertainty of future taxable income beyond 2012, the assessment of which depends largely on our operating results during our fourth quarter. We continue to believe we will be able to realize the deferred tax asset of \$587,603 based on estimated 2012 taxable income.

At the end of 2011, we had estimated net operating loss carryforwards of approximately \$16.6 million, which begin to expire in 2020. In accordance with Section 382 of the Internal Revenue Code, the use of these carryforwards may be subject to annual limitations based upon certain ownership changes of our stock that may have occurred or that may occur.

## Net loss

Due to the foregoing, our net loss in the first quarter of fiscal 2012 improved to \$1,235,266, or \$0.05 per basic and diluted share, compared to \$1,510,911, or \$0.06 per basic and diluted share, in the first quarter of the prior fiscal year.

## Liquidity and Capital Resources

Our primary uses of cash are:

- purchases of inventory, including purchases under our Supply Agreement with Amscan, as described more fully below;
  - occupancy expenses of our stores;
  - employee salaries; and
- new and temporary store openings, including acquisitions.

Our primary sources of cash are:

- cash from operating activities; and
- debt, including our Facility.

Our prospective cash flows are subject to certain trends, events and uncertainties, including demands for capital to support growth, including store acquisitions and openings and our e-commerce site, finance inventory purchases, improve our infrastructure, respond to economic conditions, and meet contractual commitments. Based on our current operating plan, we believe that anticipated revenues from operations and borrowings available under our line of credit will be sufficient to fund our operations, working capital requirements and capital expenditures through the next twelve months. In the event that our operating plan changes due to changes in our strategic plans, lower-than-expected revenues, unanticipated expenses, increased competition, unfavorable economic conditions, declines in consumer confidence and spending, or other unforeseen circumstances, our liquidity may be negatively impacted. If so, we could be required to adjust our expenditures for the remainder of 2012 to conserve working capital or raise additional capital, possibly including debt or equity financing to fund operations and our business strategy. Given the current state of the debt and equity markets and our existing capital structure, this could be difficult and expensive, and we might not be able to do so on terms acceptable to us.

## Line of Credit



On October 14, 2011, we entered into the First Amendment (“Amendment”) to the Second Amended and Restated Credit Agreement (the “Facility”) with Wells Fargo. The Facility continues the previous revolving line of credit in the amount of up to \$12,500,000 and extends the maturity date for five years to October 14, 2016. The Facility includes an option whereby we may increase the revolving line of credit up to a maximum level of \$15,000,000. The amount of credit that is available from time to time under the Facility is determined as a percentage of the value of eligible inventory plus a percentage of the value of eligible credit card receivables, as reduced by certain reserve amounts that may be required by Wells Fargo.

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Borrowings under the Facility will generally accrue interest at a margin of 0.25% over a base rate determined by Wells Fargo from time to time, or, at our election, 2.00% over the London Interbank Offered Rate (“LIBOR”). The Facility provides for letters of credit for up to a sublimit of \$2 million to be used in connection with inventory purchases and includes an unused line fee on the unused portion of the Facility. Our obligations under the Facility are secured by a lien on substantially all of our personal property.

The outstanding balances under the Facility are classified as current liabilities in the accompanying consolidated balance sheets because we are required to apply daily lock-box receipts to reduce the amount outstanding.

The Facility contains events of default customary for credit facilities of this type. Upon an event of default that is not cured or waived within any applicable cure periods, in addition to other remedies that may be available to Wells Fargo, the obligations under the line may be accelerated, outstanding letters of credit may be required to be cash collateralized and the lenders may exercise remedies to collect the balance due, including to foreclose on the collateral.

Our inventory consists of party supplies which are valued at the lower of weighted-average cost or market, which approximates FIFO (first-in, first-out) and are reduced or increased by adjustments including vendor rebates and discounts and freight costs. Our Facility availability calculation allows us to borrow against “acceptable inventory at cost”, which is based on our inventory at cost and applies adjustments that Wells Fargo has approved, which may be different than adjustments we use for valuing our inventory in our financial statements, such as the adjustment to reserve for inventory shortage. The amount of “acceptable inventory at cost” was approximately \$17,169,404 at March 31, 2012.

Our accounts receivable consist primarily of credit card receivables and vendor rebates receivable. Our Facility availability calculation allows us to borrow against “eligible credit card receivables”, which are the credit card receivables for the previous two to three days of business. The amount of “eligible credit card receivables” was approximately \$249,199 at March 31, 2012.

Our total borrowing base is determined by adding the “acceptable inventory at cost” times an agreed upon advance rate plus the “eligible credit card receivables” times an agreed upon advance rate but not to exceed our established credit limit, which was \$12,500,000 at March 31, 2012. Under the terms of the Facility, our \$12,500,000 credit limit was further reduced by (1) a minimum availability block, (2) customer deposits, (3) gift certificates, (4) merchandise credits and (5) outstanding letters of credit. The amounts outstanding under the Facility were \$5,577,293 at March 31, 2012 and \$5,366,512 at December 31, 2011, an increase of \$210,781. Our additional availability was \$4,509,213 at March 31, 2012 and \$3,129,457 at December 31, 2011.

The Facility has financial covenants that are limited to minimum availability and capital expenditures and contains various restrictive covenants, such as incurrence, payment or entry into certain indebtedness, liens, investments, acquisitions, mergers, dispositions and dividends. Under the Facility, we are required to maintain a minimum availability of 7.5% of the credit limit, except for the period January 1, 2012 through April 30, 2012, during which time the minimum availability is zero. The Facility also requires us to limit our capital expenditures to within 110% of those amounts included in our business plan, which may be updated from time to time. At March 31, 2012, we were in compliance with these financial covenants.

#### Supply Agreement with Amscan

Our Supply Agreement with Amscan gives us the right to receive more favorable pricing terms over the term of the Supply Agreement than generally were available to us under our previous terms with Amscan. In exchange, the Supply Agreement obligates us to purchase increased levels of merchandise from Amscan. Beginning with calendar

year 2008, the Supply Agreement requires us to purchase on an annual basis merchandise equal to the total number of our stores, excluding temporary stores, open during such calendar year, multiplied by \$180,000. The Supply Agreement extends until December 31, 2013.

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The Supply Agreement provides for penalties in the event we fail to attain the annual purchase commitment that would require us to pay Amscan the difference between the purchases for that year and the annual purchase commitment for that year. Under the terms of the Supply Agreement, the annual purchase commitment for any individual year can be reduced for orders placed by us but not filled by Amscan. Our purchases for 2009 fell short of the annual commitment by approximately \$368,000, which unfilled commitment was rolled into 2010. Our purchases for 2010 exceeded the minimum purchase amount commitments plus the 2009 short fall of \$368,000. Our purchases for 2011 also exceeded the minimum purchase amount commitments. The Company is not aware of any reason that would prevent it from meeting the minimum purchase requirements for the remainder of 2012 or for 2013. Although we do not expect to incur any penalties under this Supply Agreement, if they were to occur, there could be a material adverse effect on our uses and sources of cash.

#### Operating, Investing and Financing Activities

Our operating activities used cash of \$293,847 during the three months ended March 31, 2012 compared to using \$1,379,176 during the three months ended March 26, 2011, a decrease in cash used of \$1,085,329. The decrease in cash used in operating activities was primarily due to a decrease in net loss for the three months ended March 31, 2012 compared to the net loss for the same period in 2011, plus a reduction in credit card accounts receivable from December 31, 2011 to March 31, 2012.

We used \$211,796 in investing activity during the first three months of 2012 compared to \$300,653 during the first three months of 2011, a decrease of \$88,857. The cash invested in 2012 was primarily for replacement fixtures and equipment for our retail stores. The cash invested in 2011 was primarily for our new store opening in Boston, Massachusetts, point of sale register updates in our retail stores and other store improvements.

Financing activities provided \$504,443 during the first three months of 2012 compared to providing \$1,680,829 during the first three months of 2011, a decrease of \$1,176,386. The decrease was primarily due to decreased net borrowings on the line of credit during the first three months of 2012 compared to the first three months of 2011.

#### Contractual Obligations

Contractual obligations at March 31, 2012 were as follows:

	Within 1 Year	Within 2 - 3 Years	Within 4 - 5 Years	Within After 5 Years	Total
Line of credit	\$5,583,728	\$-	\$ -	\$ -	\$5,583,728
Capital lease obligations	2,850	-	-	-	2,850
Supply agreement	9,448,615	7,020,000	-	-	16,468,615
Operating leases (including retail space leases)	9,830,110	15,460,151	9,941,121		
December 31, 2010:					
Less than one year	\$3,264	(1) \$6,911	1.51%		
Greater than one year and less than five years	29,004	46,138	3.45%		
Greater than five years	31,692	30,174	5.64%		
Total	\$63,960	\$83,223	4.08%		

(1) \$3.0 million of CMBS, maturing in this category are collateralized by floating-rate loans and, as permitted under the CMBS terms, are expected to extend their respective maturity dates until at least November 2011 as the debtors

in the floating-rate structures have a contractual right to extend with options ranging from two one-year options to three one-year options. Beyond the contractual extensions, the servicer may allow further extensions of the underlying floating rate loans.

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RESOURCE CAPITAL CORP. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)  
MARCH 31, 2011  
(Unaudited)

## NOTE 4 – INVESTMENT SECURITIES AVAILABLE-FOR-SALE – (Continued)

The contractual maturities of the investment securities available-for-sale range from August 2011 to June 2022.

The following table shows the fair value and gross unrealized losses, aggregated by investment category and length of time, of those individual investment securities that have been in a continuous unrealized loss position (in thousands):

	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
March 31, 2011:						
CMBS	\$27,533	\$(3,837 )	\$9,156	\$(20,925 )	\$36,689	\$(24,762 )
Total temporarily impaired securities	\$27,533	\$(3,837 )	\$9,156	\$(20,925 )	\$36,689	\$(24,762 )
December 31, 2010:						
CMBS	\$10,134	\$(4,383 )	\$8,302	\$(22,195 )	\$18,436	\$(26,578 )
Total temporarily impaired securities	\$10,134	\$(4,383 )	\$8,302	\$(22,195 )	\$18,436	\$(26,578 )

The Company holds seven investment securities available-for-sale that have been in a loss position for more than 12 months as of March 31, 2011 and December 31, 2010. The unrealized losses in the above table are considered to be temporary impairments due to market factors and are not reflective of credit deterioration.

The determination of other-than-temporary impairment is a subjective process, and different judgments and assumptions could affect the timing of loss realization. The Company reviews its portfolios and makes other-than-temporary impairment determinations at least quarterly. The Company considers the following factors when determining if there is an other-than-temporary impairment on a security:

the length of time the market value has been less than amortized cost;

the severity of the impairment;

the expected loss with respect to the security as generated by third party software;

credit ratings from the rating agencies;

underlying credit fundamentals of the collateral backing the securities; and

whether, based upon the Company's intent, it is more likely than not that the Company will sell the security before the recovery of the amortized cost basis.

At March 31, 2011 and December 31, 2010, the Company held \$91.1 million and \$63.9 million, respectively, (net of net unrealized losses of \$14.4 million and \$19.3 million, respectively) of CMBS recorded at fair value. To determine

fair value, the Company uses two methods, either a dealer quote or an internal valuation model, depending upon the current level of market activity. As of March 31, 2011 and December 31, 2010, \$80.1 million and \$53.7 million, respectively, of investment securities available-for-sale were valued using dealer quotes and \$11.0 million and \$10.3 million, respectively, were valued using a weighted average of three measures (see Note 2).

During the three months ended March 31, 2011 and 2010, the Company did not recognize any other-than-temporary impairment on positions that supported the Company's CMBS investment. While the Company's securities classified as available-for-sale have declined in fair value on a net basis, the Company concluded that the decline continues to be temporary and does not believe that any of its securities classified as available-for-sale were other-than-temporarily impaired as of March 31, 2011 or 2010 that had not been previously classified as such. The Company performs an on-going review of third-party reports and updated financial data on the underlying properties to analyze current and projected security performance. Rating agency downgrades are considered with respect to the Company's income approach when determining other-than-temporary impairment and, when inputs are stressed, the resulting projected cash flows reflect a full recovery of principal and interest indicating no impairment.

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RESOURCE CAPITAL CORP. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)  
MARCH 31, 2011  
(Unaudited)

## NOTE 4 – INVESTMENT SECURITIES AVAILABLE-FOR-SALE – (Continued)

Changes in interest rates may also have an effect on the rate of mortgage principal prepayments and, as a result, prepayments on CMBS in the Company's investment portfolio. At March 31, 2011, the aggregate discount exceeded the aggregate premium on the Company's CMBS by approximately \$15.3 million. At December 31, 2010, the aggregate discount exceeded the aggregate premium on the Company's CMBS by approximately \$16.6 million.

## NOTE 5 – INVESTMENT SECURITIES HELD-TO-MATURITY

The following table summarizes the Company's securities held-to-maturity which are carried at amortized cost (in thousands):

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
<b>March 31, 2011:</b>				
ABS	\$29,206	\$754	\$(3,057 )	\$26,903
<b>Total</b>	<b>\$29,206</b>	<b>\$754</b>	<b>\$(3,057 )</b>	<b>\$26,903</b>
<b>December 31, 2010:</b>				
ABS	\$29,036	\$752	\$(3,847 )	\$25,941
<b>Total</b>	<b>\$29,036</b>	<b>\$752</b>	<b>\$(3,847 )</b>	<b>\$25,941</b>

The following table summarizes the estimated maturities of the Company's securities held-to-maturity according to their contractual lives (in thousands):

Contractual Life	Amortized Cost	Fair Value	Weighted Average Coupon
<b>March 31, 2011:</b>			
Greater than one year and less than five years	\$5,000	\$5,037	6.15%
Greater than five years and less than ten years	15,897	15,566	1.98%
Greater than ten years	8,309	6,300	4.13%
<b>Total</b>	<b>\$29,206</b>	<b>\$26,903</b>	
<b>December 31, 2010:</b>			
Greater than one year and less than five years	\$5,000	\$4,830	6.14%
Greater than five years and less than ten years	15,891	15,073	1.97%
Greater than ten years	8,145	6,038	4.11%
<b>Total</b>	<b>\$29,036</b>	<b>\$25,941</b>	

The following table shows the fair value and gross unrealized losses, aggregated by investment category and length of time, of those individual investment securities that have been in a continuous unrealized loss position (in thousands):



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	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
<b>March 31, 2011:</b>						
ABS	\$-	\$-	\$10,111	\$(3,057 )	\$10,111	\$(3,057 )
Total temporarily impaired securities	\$-	\$-	\$10,111	\$(3,057 )	\$10,111	\$(3,057 )
<b>December 31, 2010:</b>						
ABS	\$1,038	\$(1 )	\$11,923	\$(3,846 )	\$12,961	\$(3,847 )
Total temporarily impaired securities	\$1,038	\$(1 )	\$11,923	\$(3,846 )	\$12,961	\$(3,847 )

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## NOTE 5 – INVESTMENT SECURITIES HELD-TO-MATURITY

The Company holds 10 and 12 investment securities held-to-maturity that have been in a loss position for more than 12 months as of March 31, 2011 and December 31, 2010, respectively. The unrealized losses in the above table are considered to be temporary impairments due to market factors and are not reflective of credit deterioration. The Company does not believe that any of its investments classified as held-to-maturity were other-than-temporarily impaired as of March 31, 2011.

The determination of other-than-temporary impairment is a subjective process, and different judgments and assumptions could affect the timing of loss realization. The Company reviews its portfolios and makes other-than-temporary impairment determinations at least quarterly. The Company considers the following factors when determining if there is an other-than-temporary impairment on a security:

- the severity of the impairment;
- the expected loss of the security as generated by third party software;
- original and current credit ratings from the rating agencies;
- underlying credit fundamentals of the collateral backing the securities; and
- third-party support for default, recovery, prepayment speed and reinvestment price assumptions.

## NOTE 6 – LOANS HELD FOR INVESTMENT

The following is a summary of the Company's loans (in thousands):

Loan Description	Principal	Unamortized (Discount) Premium (1)	Carrying Value (2)
<b>March 31, 2011:</b>			
Bank loans (3)	\$899,165	\$ (23,365 )	\$875,800
<b>Commercial real estate loans:</b>			
Whole loans (3)	460,539	(458 )	460,081
B notes (3)	55,327	(160 )	55,167
Mezzanine loans (3)	115,326	84	115,410
Total commercial real estate loans	631,192	(534 )	630,658
Subtotal loans before allowances	1,530,357	(23,899 )	1,506,458
Allowance for loan loss	(27,669 )	–	(27,669 )
<b>Total</b>	<b>\$1,502,688</b>	<b>\$ (23,899 )</b>	<b>\$1,478,789</b>
<b>December 31, 2010:</b>			
Bank loans (3)	\$887,667	\$ (27,204 )	\$860,463
<b>Commercial real estate loans:</b>			
Whole loans	441,706	(334 )	441,372

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B notes	57,613	(162 )	57,451
Mezzanine loans (3)	146,668	143	146,811
Total commercial real estate loans	645,987	(353 )	645,634
Subtotal loans before allowances	1,533,654	(27,557 )	1,506,097
Allowance for loan loss	(34,233 )	–	(34,233 )
Total	\$1,499,421	\$ (27,557 )	\$1,471,864

(1) Amounts include deferred amendment fees of \$276,000 and \$636,000 being amortized over the life of the bank loans and \$79,000 and \$681,000 being amortized over the life of the commercial real estate loans as of March 31, 2011 and December 31, 2010, respectively.

(2) Substantially all loans are pledged as collateral under various borrowings at March 31, 2011 and December 31, 2010, respectively.

(3) Amounts include \$9.9 million of bank loans, \$676,000 of whole loans, \$12.8 million of B notes and \$19.5 million of mezzanine loans held for sale as of March 31, 2011, and \$4.0 million of bank loans and \$24.6 million of mezzanine loans held for sale as of December 31, 2010.

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## NOTE 6 – LOANS HELD FOR INVESTMENT – (Continued)

As of March 31, 2011 and December 31, 2010, approximately 41.7% and 38.0%, respectively, of the Company's commercial real estate loan portfolio was concentrated in commercial real estate loans located in California and 9.5% and 10.4%, respectively, were concentrated in New York. As of March 31, 2011 and December 31, 2010, approximately 11.1% and 10.7%, respectively, of the Company's bank loan portfolio was concentrated in the collective industry grouping of healthcare, education and childcare.

At March 31, 2011, the Company's bank loan portfolio consisted of \$874.0 million (net of allowance of \$1.8 million) of floating rate loans, which bear interest ranging between the London Interbank Offered Rate ("LIBOR") plus 0.5% and LIBOR plus 9.5% with maturity dates ranging from July 2011 to March 2018.

At December 31, 2010, the Company's bank loan portfolio consisted of \$857.9 million (net of allowance of \$2.6 million) of floating rate loans, which bear interest ranging between the LIBOR plus 0.5% and LIBOR plus 9.5% with maturity dates ranging from March 2011 to December 2017.

The following is a summary of the weighted average life of the Company's bank loans, at amortized cost (in thousands):

	March 31, 2011	December 31, 2010
Less than one year	\$7,213	\$4,245
Greater than one year and less than five years	593,136	643,699
Five years or greater	275,451	212,519
	\$875,800	\$860,463

The following is a summary of the Company's commercial real estate loans (in thousands):

Description	Quantity	Amortized Cost	Contracted Interest Rates	Maturity Dates (4)
March 31, 2011:				
Whole loans, floating rate (1)	27	\$ 460,081	LIBOR plus 1.50% to LIBOR plus 5.75%	May 2011 to May 2017
B notes, floating rate	2	24,242	LIBOR plus 2.50% to LIBOR plus 3.01%	July 2011 to October 2011
B notes, fixed rate	2	30,925	7.00% to 8.68%	July 2011 to April 2016
Mezzanine loans, floating rate	5	81,878	LIBOR plus 2.20% to	May 2011 to January 2013

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			LIBOR plus 3.00%	
Mezzanine loans, fixed rate (2)	4	33,532	8.65% to 11.00%	January 2016 to September 2016
<b>Total (3)</b>	<b>40</b>	<b>\$ 630,658</b>		

December 31, 2010:

			LIBOR plus 1.50% to LIBOR plus 5.75%	May 2011 to January 2018
Whole loans, floating rate (1)	25	\$ 441,372	LIBOR plus 2.50% to LIBOR plus 3.01%	July 2011 to October 2011
B notes, floating rate	2	26,485	7.00% to 8.68%	July 2011 to April 2016
B notes, fixed rate	2	30,966	LIBOR plus 2.15% to LIBOR plus 3.00%	May 2011 to January 2013
Mezzanine loans, floating rate	6	93,266	8.14% to 11.00%	January 2016 to September 2016
Mezzanine loans, fixed rate (2)	5	53,545		
<b>Total (3)</b>	<b>40</b>	<b>\$ 645,634</b>		

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## NOTE 6 – LOANS HELD FOR INVESTMENT – (Continued)

- (1) Whole loans had \$9.1 million and \$5.0 million in unfunded loan commitments as of March 31, 2011 and December 31, 2010, respectively. These commitments are funded as the borrowers require additional funding and have satisfied the requirements to obtain this additional funding.
- (2) Fixed rate mezzanine loan dates exclude a loan that matured in May 2010 and is in default and has been on non-accrual status as of December 31, 2010. This loan was written-off as of March 31, 2011.
- (3) The total does not include an allowance for loan losses of \$25.9 million and \$31.6 million recorded as of March 31, 2011 and December 31, 2010, respectively.
- (4) Maturity dates do not include possible extension options that may be available to the borrowers.

Subsequent to March 31, 2011, the Company entered into and completed sale agreements for two commercial real estate loans. One loan is secured by a hotel portfolio in various locations that the Company sold at 85% of par, resulting in a loss of \$2.25 million of which \$235,000 had been previously allocated as part of its general reserve. The second loan is secured by an office tower in New York City that the Company sold at par with transaction costs resulting in a loss of \$656,000. The third loan with a fair value of \$676,000 is secured by a pad for retail use in Arizona. The Company expects a sale to occur during 2011. The Company classified these loans as loans held for sale as of March 31, 2011.

The following is a summary of the weighted average life of the Company's commercial real estate loans, at amortized cost (in thousands):

Description	2011	2012	2013 and Thereafter	Total
March 31, 2011:				
B notes	\$38,659	\$–	\$16,508	\$55,167
Mezzanine loans	–	23,289	92,121	115,410
Whole loans	107,775	87,090	265,216	460,081
Total (2)	\$146,434	\$110,379	\$373,845	\$630,658
December 31, 2010:				
B notes	\$40,913	\$–	\$16,538	\$57,451
Mezzanine loans (1)	–	34,676	107,135	141,811
Whole loans	108,303	87,084	245,985	441,372
Total (2)	\$149,216	\$121,760	\$369,658	\$640,634

(1) Mezzanine loans exclude one loan with an amortized cost of \$5.0 million which matured in May 2010 and is in default.

(2) Weighted average life of commercial real estate loans assumes full exercise of extension options available to borrowers.

The following is a summary of the allocation of the allowance for loan loss with respect to the Company's commercial real estate and bank loans (in thousands, except percentages) by asset class:

Description	Allowance for Loan Loss	Percentage of Total Allowance
March 31, 2011:		
B notes	\$621	2.2%
Mezzanine loans	3,718	13.5%
Whole loans	21,499	77.7%
Bank loans	1,831	6.6%
Total	\$27,669	
December 31, 2010:		
B notes	\$899	2.6%
Mezzanine loans	8,553	25.0%
Whole loans	22,165	64.8%
Bank loans	2,616	7.6%
Total	\$34,233	

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## NOTE 6 – LOANS HELD FOR INVESTMENT – (Continued)

As of March 31, 2011, the Company had recorded an allowance for loan losses of \$27.7 million consisting of a \$1.8 million allowance on the Company's bank loan portfolio and a \$25.9 million allowance on the Company's commercial real estate portfolio as a result of the impairment of one bank loan and eight commercial real estate loans as well as the provision of a general reserve with respect to these portfolios.

As of December 31, 2010, the Company had recorded an allowance for loan losses of \$34.2 million consisting of a \$2.6 million allowance on the Company's bank loan portfolio and a \$31.6 million allowance on the Company's commercial real estate portfolio as a result of the impairment of one bank loan and eight commercial real estate loans as well as the provision of a general reserve with respect to these portfolios.

## NOTE 7 – FINANCING RECEIVABLES

The following tables show the allowance for loan and lease receivable losses and recorded investments in loans and lease receivables (in thousands):

	Commercial Real Estate Loans	Bank Loans	Loans Receivable-Related Party	Total
March 31, 2011:				
Allowance for losses at January 1, 2011	\$ 31,617	\$ 2,616	\$ –	\$ 34,233
Provision for (reversal of) loan loss	3,121	(515 )	–	2,606
Loans charged-off	(8,900 )	(270 )	–	(9,170 )
Recoveries	–	–	–	–
Allowance for losses at March 31, 2011	\$ 25,838	\$ 1,831	\$ –	\$ 27,669
Ending balance:				
Individually evaluated for impairment	\$ 15,300	\$ 112	\$ –	\$ 15,412
Collectively evaluated for impairment	\$ 10,538	\$ 1,719	\$ –	\$ 12,257
Loans acquired with deteriorated credit quality	\$ –	\$ –	\$ –	\$ –
Loans:				
Ending balance:				
Individually evaluated for impairment	\$ 36,000	\$ 362	\$ –	\$ 36,362
Collectively evaluated for impairment	\$ 594,658	\$ 875,438	\$ 9,689	\$ 1,479,785
Loans acquired with	\$ –	\$ –	\$ –	\$ –



deteriorated credit quality

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## NOTE 7 –FINANCING RECEIVABLES – (Continued)

	Commercial Real Estate Loans	Bank Loans	Lease Receivables	Loans Receivable-Related Party	Total
December 31, 2010:					
Allowance for losses at January 1, 2010	\$ 29,297	\$ 17,825	\$ 1,140	\$ –	\$ 48,262
Provision for (reversal of) loan loss	44,357	(1,348 )	312	–	43,321
Loans charged-off	(42,037 )	(13,861 )	(1,432 )	–	(57,330 )
Recoveries	–	–	50	–	50
Allowance for losses at December 31, 2010	\$ 31,617	\$ 2,616	\$ 70	\$ –	\$ 34,303
Ending balance:					
Individually evaluated for impairment	\$ 20,844	\$ 112	\$ –	\$ –	\$ 20,956
Collectively evaluated for impairment	\$ 10,773	\$ 2,504	\$ 70	\$ –	\$ 13,347
Loans acquired with deteriorated credit quality	\$ –	\$ –	\$ –	\$ –	\$ –
Loans:					
Ending balance:					
Individually evaluated for impairment	\$ 42,219	\$ 362	\$ 10,024	\$ –	\$ 52,605
Collectively evaluated for impairment	\$ 603,415	\$ 860,101	\$ 99,658	\$ 9,927	\$ 1,573,101
Loans acquired with deteriorated credit quality	\$ –	\$ –	\$ –	\$ –	\$ –

## Credit quality indicators

## Bank Loans

The Company uses a risk grading matrix to assign grades to bank loans. Loans are graded at inception and updates to assigned grades are made continually as new information is received. Loans are graded on a scale of 1-5 with 1 representing the Company's highest rating and 5 representing its lowest rating. We also designate loans that are sold after the period then ended as such at their fair market value, net of any allowances and costs associated with the loan sales. The Company considers such things as performance of the underlying company, liquidity, collectability of interest, enterprise valuation, default probability, ratings from rating agencies, and industry dynamics.

Credit risk profiles of bank loans were as follows (in thousands):

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	Rating 1	Rating 2	Rating 3	Rating 4	Rating 5	Held for Sale	Total
As of March 31, 2011:							
Bank loans	\$787,108	\$31,150	\$41,330	\$5,960	\$362	\$9,890	\$875,800
As of December 31, 2010:							
Bank loans	\$759,161	\$43,858	\$45,115	\$7,940	\$362	\$4,027	\$860,463

All of the Company's bank loans are performing with the exception of one loan with a par amount of \$362,000 which has been in default since September 2010.

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## NOTE 7 –FINANCING RECEIVABLES – (Continued)

## Commercial Real Estate Loans

The Company uses a risk grading matrix to assign grades to commercial real estate loans. Loans are graded at inception and updates to assigned grades are made continually as new information is received. Loans are graded on a scale of 1-4 with 1 representing the Company's highest rating and 4 representing its lowest rating. We also designate loans that are sold after the period then ended as such at their fair market value, net of any allowances and costs associated with the loan sales. In addition to the underlying performance of the loan collateral, the Company considers such things as the strength of underlying sponsorship, payment history, collectability of interest, structural credit enhancements, market trends and loan terms.

Credit risk profiles of commercial real estate loans were as follows (in thousands):

	Rating 1	Rating 2	Rating 3	Rating 4	Held for Sale	Total
As of March 31, 2011:						
Whole loans	\$ 169,503	\$ 45,559	\$ 208,343	\$ 36,000	\$ 676	\$ 460,081
B notes	16,508	11,492	14,417	–	12,750	55,167
Mezzanine loans	7,525	33,805	54,552	–	19,528	115,410
	\$ 193,536	\$ 90,856	\$ 277,312	\$ 36,000	\$ 32,954	\$ 630,658
As of December 31, 2010:						
Whole loans	\$ 123,350	\$ 16,143	\$ 264,660	\$ 37,219	\$ –	\$ 441,372
B notes	16,538	–	40,913	–	–	57,451
Mezzanine loans	32,635	–	84,610	5,000	24,566	146,811
	\$ 172,523	\$ 16,143	\$ 390,183	\$ 42,219	\$ 24,566	\$ 645,634

All of the Company's commercial real estate loans are performing with the exception of one loan with a par amount of \$5.0 million which has been in default since May 2010. This position was charged off as of March 31, 2011.

## Loan and Lease Receivable Portfolios Aging Analysis

The following tables show the loan and lease receivable portfolio aging analysis indicated at cost basis (in thousands):

	30-59 Days	60-89 Days	Greater than 90 Days	Total Past Due	Current	Total Loans Receivable	Total Loans > 90 Days and Accruing
March 31, 2011:							
Whole loans	\$ –	\$ –	\$ –	\$ –	\$ 460,081	\$ 460,081	\$ –
B notes	–	–	–	–	55,167	55,167	–
	–	–	–	–	115,410	115,410	–

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Mezzanine loans								
Bank loans	–	–	362	362	875,438	875,800	–	
Loans receivable-related party	–	–	–	–	9,689	9,689	–	
Total loans	\$ –	\$ –	\$ 362	\$ 362	\$ 1,515,785	\$ 1,516,147	\$ –	

December 31, 2010:

Whole loans	\$ –	\$ –	\$ –	\$ –	\$ 441,372	\$ 441,372	\$ –	
B notes	–	–	–	–	57,451	57,451	–	
Mezzanine loans	–	–	5,000	5,000	141,811	146,811	–	
Bank loans	–	–	–	–	860,463	860,463	–	
Lease receivables	630	237	829	1,696	107,986	109,682	–	
Loans receivable-related party	–	–	–	–	9,927	9,927	–	
Total loans	\$ 630	\$ 237	\$ 5,829	\$ 6,696	\$ 1,619,010	\$ 1,625,706	\$ –	

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## NOTE 7 –FINANCING RECEIVABLES – (Continued)

## Impaired Loans and Lease Receivables

The following tables show impaired loans and lease receivables indicated (in thousands):

	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Average Investment in Impaired Loans	Interest Income Recognized
<b>March 31, 2011:</b>					
Loans and lease receivables without a specific valuation allowance:					
Whole loans	\$ 112,433 (1)	\$ 112,433	\$ –	\$ 111,959	\$ 513
B notes	–	–	–	–	–
Mezzanine loans	–	–	–	–	–
Bank loans	–	–	–	–	–
Loans and lease receivables with a specific valuation allowance:					
Whole loans	36,000	36,000	(15,300 )	35,880	227
B notes	–	–	–	–	–
Mezzanine loans	–	–	–	5,000	–
Bank loans	362	362	(112 )	362	–
<b>Total:</b>					
Whole loans	\$ 148,433	\$ 148,433	\$ (15,300 )	\$ 147,839	\$ 740
B notes	–	–	–	–	–
Mezzanine loans	–	–	–	5,000	–
Bank loans	362	362	(112 )	362	–
	\$ 148,795	\$ 148,795	\$ (15,412 )	\$ 153,201	\$ 740
<b>December 31, 2010:</b>					
Loans and lease receivables without a specific valuation allowance:					
Whole loans	\$ 111,401 (1)	\$ 111,401	\$ –	\$ 58,058	\$ 1,133
B notes	–	–	–	–	–
Mezzanine loans	–	–	–	–	–
Bank loans	–	–	–	–	–
Lease receivables	–	–	–	–	–
Loans and lease receivables with a specific valuation allowance:					
Whole loans	37,219	37,219	(15,844 )	36,740	993
B notes	–	–	–	–	–

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Mezzanine loans	5,000	5,000	(5,000 )	5,000	–
Bank loans	362	362	(112 )	8,971	–
Lease receivables	10,024	10,024	(4,107 )	4,791	–
<b>Total:</b>					
Whole loans	\$ 148,620	\$ 148,620	\$ (15,844 )	\$ 94,798	\$ 2,126
B notes	–	–	–	–	–
Mezzanine loans	5,000	5,000	(5,000 )	5,000	–
Bank loans	362	362	(112 )	8,971	–
Lease receivables	10,024	10,024	(4,107 )	4,791	–
	\$ 164,006	\$ 164,006	\$ (25,063 )	\$ 113,560	\$ 2,126

(1) Specific allowances were not taken on whole loans with a par value of \$112.4 million and \$111.4 million as of March 31, 2011 and December 31, 2010, respectively which were evaluated and deemed to be TDRs. These TDRs do not have an associated specific loan loss allowance because the principal and interest amount is considered recoverable based on expected collateral performance and / or guarantees made by the borrowers.

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## NOTE 8 – INTANGIBLE ASSETS

Intangible assets represent identifiable intangible assets acquired as a result of the Company's acquisition of RCAM in February 2011. The Company amortizes identified intangible assets to expense over their estimated lives using the straight-line method. The Company evaluates intangible assets for impairment as events and circumstances change. The Company expects to record amortization expense of intangible assets of \$2.2 million for the year ended December 31, 2011, \$2.6 million for the years ended December 31, 2012 through December 31, 2015 and \$2.5 million for the year ended December 31, 2016. The weighted average amortization period is eight years at March 31, 2011 and the accumulated amortization at March 31, 2011 was \$253,000.

## NOTE 9 – BORROWINGS

The Company historically has financed the acquisition of its investments, including investment securities, loans and lease receivables, primarily through the use of secured and unsecured borrowings in the form of CDOs, securitized notes, repurchase agreements, secured term facilities, warehouse facilities, trust preferred securities issuances and other secured and unsecured borrowings. Certain information with respect to the Company's borrowings at March 31, 2011 and December 31, 2010 is summarized in the following table (in thousands, except percentages):

	Outstanding Borrowings	Weighted Average Borrowing Rate	Weighted Average Remaining Maturity	Value of Collateral
<b>March 31, 2011:</b>				
RREF CDO 2006-1 Senior Notes (1)	\$ 173,182	1.32%	35.4 years	\$ 229,859
RREF CDO 2007-1 Senior Notes (2)	325,228	0.81%	35.5 years	361,186
Apidos CDO I Senior Notes (3)	319,911	0.88%	6.3 years	316,219
Apidos CDO III Senior Notes (4)	260,813	0.76%	9.2 years	260,709
Apidos Cinco CDO Senior Notes (5)	319,519	0.82%	9.1 years	325,559
Unsecured Junior Subordinated Debentures (7)	50,431	6.26%	25.4 years	–
Repurchase Agreements (8)	14,617	1.51%	18.0 days	17,522
<b>Total</b>	<b>\$ 1,463,701</b>	<b>1.07%</b>	<b>18.0 years</b>	<b>\$ 1,511,054</b>
<b>December 31, 2010:</b>				
RREF CDO 2006-1 Senior Notes (1)	\$ 173,053	1.33%	35.6 years	\$ 215,063
RREF CDO 2007-1 Senior Notes (2)	325,025	0.82%	35.8 years	367,792
Apidos CDO I Senior Notes (3)	319,748	0.87%	6.6 years	309,746
Apidos CDO III Senior Notes (4)	260,682	0.75%	9.5 years	250,309
Apidos Cinco CDO Senior Notes (5)	319,373	0.79%	9.4 years	319,563
Equipment Contract Backed Notes, Series 2010-2 (6)	95,016	5.00%	5.4 years	109,612
Unsecured Junior Subordinated Debentures (7)	50,354	6.24%	25.7 years	–
<b>Total</b>	<b>\$ 1,543,251</b>	<b>1.30%</b>	<b>17.6 years</b>	<b>\$ 1,572,085</b>



- 
- (1) Amount represents principal outstanding of \$174.9 million and \$174.9 million less unamortized issuance costs of \$1.7 million and \$1.8 million as of March 31, 2011 and December 31, 2010, respectively. This CDO transaction closed in August 2006.
  - (2) Amount represents principal outstanding of \$328.6 million and \$328.5 million less unamortized issuance costs of \$3.4 million and \$3.5 million as of March 31, 2011 and December 31, 2010, respectively. This CDO transaction closed in June 2007.
  - (3) Amount represents principal outstanding of \$321.5 million less unamortized issuance costs of \$1.6 million as of March 31, 2011 and \$1.8 million as of December 31, 2010. This CDO transaction closed in August 2005.
  - (4) Amount represents principal outstanding of \$262.5 million less unamortized issuance costs of \$1.7 million as of March 31, 2011 and \$1.8 million as of December 31, 2010. This CDO transaction closed in May 2006.
  - (5) Amount represents principal outstanding of \$322.0 million less unamortized issuance costs of \$2.5 million as of March 31, 2011 and \$2.6 million as of December 31, 2010. This CDO transaction closed in May 2007.
  - (6) Amount represents principal outstanding of \$96.1 million less unamortized issuance costs of \$1.1 million as of December 31, 2010. There was no outstanding balance as of March 31, 2011.
  - (7) Amount represents junior subordinated debentures issued to RCT I and RCT II in May 2006 and September 2006, respectively.
  - (8) Amount represents principal outstanding of \$15.1 million less unamortized deferred debt costs of \$498,000 related to a CMBS repurchase facility as of March 31, 2011.

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NOTE 9 – BORROWINGS – (Continued)

Collateralized Debt Obligations

Resource Real Estate Funding CDO 2007-1

In June 2007, the Company closed RREF CDO 2007-1, a \$500.0 million CDO transaction that provides financing for commercial real estate loans and commercial mortgage-backed securities. The investments held by RREF CDO 2007-1 collateralize the debt it issued and, as a result, the investments are not available to the Company, its creditors or stockholders. RREF CDO 2007-1 issued a total of \$265.6 million of senior notes at par to unrelated investors. RCC Real Estate purchased 100% of the class H senior notes (rated BBB+:Fitch), class K senior notes (rated BBB-:Fitch), class L senior notes (rated BB:Fitch) and class M senior notes (rated B: Fitch) for \$68.0 million. In addition, Resource Real Estate Funding 2007-1 CDO Investor, LLC, a subsidiary of RCC Real Estate, purchased a \$41.3 million equity interest representing 100% of the outstanding preference shares. The senior notes purchased by RCC Real Estate are subordinated in right of payment to all other senior notes issued by RREF CDO 2007-1 but are senior in right of payment to the preference shares. The equity interest is subordinated in right of payment to all other securities issued by RREF CDO 2007-1.

The senior notes issued to investors by RREF CDO 2007-1 consist of the following classes: (i) \$180.0 million of class A-1 notes bearing interest at one-month LIBOR plus 0.28%; (ii) \$50.0 million of unissued class A-1R notes, which allow the CDO to fund future funding obligations under the existing whole loan participations that have future funding commitments; the undrawn balance of the class A-1R notes will accrue a commitment fee at a rate per annum equal to 0.18%, the drawn balance will bear interest at one-month LIBOR plus 0.32%; (iii) \$57.5 million of class A-2 notes bearing interest at one-month LIBOR plus 0.46%; (iv) \$22.5 million of class B notes bearing interest at one-month LIBOR plus 0.80%; (v) \$7.0 million of class C notes bearing interest at a fixed rate of 6.423%; (vi) \$26.8 million of class D notes bearing interest at one-month LIBOR plus 0.95%; (vii) \$11.9 million of class E notes bearing interest at one-month LIBOR plus 1.15%; (viii) \$11.9 million of class F notes bearing interest at one-month LIBOR plus 1.30%; (ix) \$11.3 million of class G notes bearing interest at one-month LIBOR plus 1.55%; (x) \$11.3 million of class H notes bearing interest at one-month LIBOR plus 2.30%; (xi) \$11.3 million of class J notes bearing interest at one-month LIBOR plus 2.95%; (xii) \$10.0 million of class K notes bearing interest at one-month LIBOR plus 3.25%; (xiii) \$18.8 million of class L notes bearing interest at a fixed rate of 7.50% and (xiv) \$28.8 million of class M notes bearing interest at a fixed rate of 8.50%. All of the notes issued mature in September 2046, although the Company has the right to call the notes anytime after July 2017 until maturity. The weighted average interest rate on all notes issued to outside investors and net of repurchased notes was 0.81% and 0.82% at March 31, 2011 and December 31, 2010, respectively.

During the three months ended March 31, 2011, the Company did not repurchase any notes. During the three months ended March 31, 2010 the Company repurchased \$250,000 of the Class J Notes in RREF CDO 2007-1 at a weighted average price of 9.00% to par which resulted in a \$228,000 gain, reported as a part of the gain on the extinguishment of debt in the consolidated statements of income.

As a result of the Company's ownership of senior notes, both the notes repurchased subsequent to closing and those retained at the CDO's closing eliminate in consolidation.



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NOTE 9 – BORROWINGS – (Continued)

Resource Real Estate Funding CDO 2006-1

In August 2006, the Company closed RREF CDO 2006-1, a \$345.0 million CDO transaction that provides financing for commercial real estate loans. The investments held by RREF CDO 2006-1 collateralize the debt it issued and, as a result, the investments are not available to the Company, its creditors or stockholders. RREF CDO 2006-1 issued a total of \$308.7 million of senior notes at par to investors of which RCC Real Estate purchased 100% of the class J senior notes (rated BB: Fitch) and class K senior notes (rated B:Fitch) for \$43.1 million. In addition, Resource Real Estate Funding 2006-1 CDO Investor, LLC, a subsidiary of RCC Real Estate, purchased a \$36.3 million equity interest representing 100% of the outstanding preference shares. The senior notes purchased by RCC Real Estate are subordinated in right of payment to all other senior notes issued by RREF CDO 2006-1 but are senior in right of payment to the preference shares. The equity interest is subordinated in right of payment to all other securities issued by RREF CDO 2006-1.

The senior notes issued to investors by RREF CDO 2006-1 consist of the following classes: (i) \$129.4 million of class A-1 notes bearing interest at one-month LIBOR plus 0.32%; (ii) \$17.4 million of class A-2 notes bearing interest at one-month LIBOR plus 0.35%; (iii) \$5.0 million of class A-2 notes bearing interest at a fixed rate of 5.842%; (iv) \$6.9 million of class B notes bearing interest at one-month LIBOR plus 0.40%; (v) \$20.7 million of class C notes bearing interest at one-month LIBOR plus 0.62%; (vi) \$15.5 million of class D notes bearing interest at one-month LIBOR plus 0.80%; (vii) \$20.7 million of class E notes bearing interest at one-month LIBOR plus 1.30%; (viii) \$19.8 million of class F notes bearing interest at one-month LIBOR plus 1.60%; (ix) \$17.3 million of class G notes bearing interest at one-month LIBOR plus 1.90%; (x) \$12.9 million of class H notes bearing interest at one-month LIBOR plus 3.75%, (xi) \$14.7 million of Class J notes bearing interest at a fixed rate of 6.00% and (xii) \$28.4 million of Class K notes bearing interest at a fixed rate of 6.00%. As a result of the Company's ownership of the Class J and K senior notes, these notes eliminate in consolidation. All of the notes issued mature in August 2046, although the Company has the right to call the notes anytime after August 2016 until maturity. The weighted average interest rate on all notes issued to outside investors and net of repurchased notes was 1.32% and 1.33% at March 31, 2011 and December 31, 2010, respectively.

During the three months ended March 31, 2011, the Company did not repurchase any notes. During three months ended March 31, 2010 the Company repurchased \$20.0 million of the Class A-1 notes in RREF CDO 2006-1 at a weighted average price of 68.0% to par which resulted in a \$6.4 million gain reported as a gain on the extinguishment of debt in the consolidated statements of income.

As a result of the Company's ownership of senior notes, both the notes repurchased subsequent to closing and those retained at the CDO's closing eliminate in consolidation.

Equipment Contract Backed Notes, Series 2010-2

In May 2010, the Company acquired Equipment Contract Backed Notes, Series 2010-2, issued by LEAF Equipment Leasing Income Fund III, L.P. ("LEAF Funding 3"), a \$120.0 million transaction that provided financing for leases. The investments held by LEAF Funding 3 collateralize the debt it issued and, as a result, the investments were not available to the Company, its creditors or stockholders. LEAF Funding 3 issued a total of \$120.0 million of senior

notes at a weighted average price of \$93.52 to unrelated investors generating proceeds of \$112.2 million. Before contributing its interest in LEAF Funding 3 to LEAF Commercial Capital, described below, the Company amortized the discount over the lives of the notes using the effective yield method, adjusted for the effects of estimated prepayments on the notes. The Company had \$21.0 million of equity invested in LEAF Funding 3 as of December 31, 2010.

On January 4, 2011, the Company made a preferred investment in LCC and contributed its equity in LEAF Funding 3 and related debt as part of that investment.

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NOTE 9 – BORROWINGS – (Continued)

Collateralized Debt Obligations – (Continued)

Apidos Cinco CDO

In May 2007, the Company closed Apidos Cinco CDO, a \$350.0 million CDO transaction that provides financing for bank loans. The investments held by Apidos Cinco CDO collateralize the debt it issued and, as a result, the investments are not available to the Company, its creditors or stockholders. Apidos Cinco CDO issued a total of \$322.0 million of senior notes at par to investors and RCC commercial purchased a \$28.0 million equity interest representing 100% of the outstanding preference shares. The equity interest is subordinated in right of payment to all other securities issued by Apidos Cinco CDO.

The senior notes issued to investors by Apidos Cinco CDO consist of the following classes: (i) \$37.5 million of class A-1 notes bearing interest at LIBOR plus 0.24%; (ii) \$200.0 million of class A-2a notes bearing interest at LIBOR plus 0.23%; (iii) \$22.5 million of class A-2b notes bearing interest at LIBOR plus 0.32%; (iv) \$19.0 million of class A-3 notes bearing interest at LIBOR plus 0.42%; (v) \$18.0 million of class B notes bearing interest at LIBOR plus 0.80%; (vi) \$14.0 million of class C notes bearing interest at LIBOR plus 2.25% and (vii) \$11.0 million of class D notes bearing interest at LIBOR plus 4.25%. All of the notes issued mature on May 14, 2020, although the Company has the right to call the notes anytime after May 14, 2011 until maturity. The weighted average interest rate on all notes was 0.82% and 0.79% at March 31, 2011 and December 31, 2010, respectively.

Apidos CDO III

In May 2006, the Company closed Apidos CDO III, a \$285.5 million CDO transaction that provides financing for bank loans. The investments held by Apidos CDO III collateralize the debt it issued and, as a result, the investments are not available to the Company, its creditors or stockholders. Apidos CDO III issued a total of \$262.5 million of senior notes at par to investors and RCC Commercial purchased a \$23.0 million equity interest representing 100% of the outstanding preference shares. The equity interest is subordinated in right of payment to all other securities issued by Apidos CDO III.

The senior notes issued to investors by Apidos CDO III consist of the following classes: (i) \$212.0 million of class A-1 notes bearing interest at 3-month LIBOR plus 0.26%; (ii) \$19.0 million of class A-2 notes bearing interest at 3-month LIBOR plus 0.45%; (iii) \$15.0 million of class B notes bearing interest at 3-month LIBOR plus 0.75%; (iv) \$10.5 million of class C notes bearing interest at 3-month LIBOR plus 1.75%; and (v) \$6.0 million of class D notes bearing interest at 3-month LIBOR plus 4.25%. All of the notes issued mature on June 12, 2020, although the Company has the right to call the notes anytime after June 12, 2011 until maturity. The weighted average interest rate on all notes was 0.76% and 0.75% at March 31, 2011 and December 31, 2010, respectively.

Apidos CDO I

In August 2005, the Company closed Apidos CDO I, a \$350.0 million CDO transaction that provides financing for bank loans. The investments held by Apidos CDO I collateralize the debt it issued and, as a result, the investments are not available to the Company, its creditors or stockholders. Apidos CDO I issued a total of \$321.5 million of senior

notes at par to investors and RCC Commercial purchased a \$28.5 million equity interest representing 100% of the outstanding preference shares. The equity interest is subordinated in right of payment to all other securities issued by Apidos CDO I.

The senior notes issued to investors by Apidos CDO I consist of the following classes: (i) \$265.0 million of class A-1 notes bearing interest at 3-month LIBOR plus 0.26%; (ii) \$15.0 million of class A-2 notes bearing interest at 3-month LIBOR plus 0.42%; (iii) \$20.5 million of class B notes bearing interest at 3-month LIBOR plus 0.75%; (iv) \$13.0 million of class C notes bearing interest at 3-month LIBOR plus 1.85%; and (v) \$8.0 million of class D notes bearing interest at a fixed rate of 9.251%. All of the notes issued mature on July 27, 2017, although the Company has the right to call the notes anytime after July 27, 2010 until maturity. The weighted average interest rate on all notes was 0.88% and 0.87% at March 31, 2011 and December 31, 2010, respectively.

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NOTE 9 – BORROWINGS – (Continued)

Unsecured Junior Subordinated Debentures

In May 2006 and September 2006, the Company formed RCT I and RCT II, respectively, for the sole purpose of issuing and selling capital securities representing preferred beneficial interests. Although the Company owns 100% of the common securities of RCT I and RCT II, RCT I and RCT II are not consolidated into the Company's consolidated financial statements because the Company is not deemed to be the primary beneficiary of these entities. In connection with the issuance and sale of the capital securities, the Company issued junior subordinated debentures to RCT I and RCT II of \$25.8 million each, representing the Company's maximum exposure to loss. The debt issuance costs associated with the junior subordinated debentures for RCT I and RCT II are included in borrowings and are being amortized into interest expense in the consolidated statements of income using the effective yield method over a ten year period.

In October 2009, the Company amended the trust agreements and unsecured junior subordinated debentures held by RCT I and RCT II with a total value outstanding of \$51.5 million. The amendment provided for an interest rate increase of 2% (from LIBOR plus 3.95% to LIBOR plus 5.95%) on both issuances for a period of two years and a one-time restructuring fee of \$250,000 in exchange for the waiver of financial covenants under the Company's guarantee. The debt issuance costs associated with the junior subordinated debentures for RCT I and RCT II at March 31, 2011 were \$551,000 and \$566,000, respectively. The debt issuance costs associated with the junior subordinated debentures for RCT I and RCT II at December 31, 2010 were \$590,000 and \$604,000, respectively. The interest rate adjustment took effect as of October 1, 2009 and expires on September 30, 2011. The rates for RCT I and RCT II, at March 31, 2011, were 6.26% and 6.25%, respectively. The rates for RCT I and RCT II, at December 31, 2010, were 6.25% and 6.24%, respectively. The covenant waiver expires on January 1, 2012.

The rights of holders of common securities of RCT I and RCT II are subordinate to the rights of the holders of capital securities only in the event of a default; otherwise, the common securities' economic and voting rights are pari passu with the capital securities. The capital and common securities of RCT I and RCT II are subject to mandatory redemption upon the maturity or call of the junior subordinated debentures held by each. Unless earlier dissolved, RCT I will dissolve on May 25, 2041 and RCT II will dissolve on September 29, 2041. The junior subordinated debentures are the sole assets of RCT I and RCT II, mature on June 30, 2036 and October 30, 2036, respectively, and may be called at par by the Company any time after June 30, 2011 and October 30, 2011, respectively. The Company records its investments in RCT I and RCT II's common securities of \$774,000 each as investments in unconsolidated trusts and records dividend income upon declaration by RCT I and RCT II.

Repurchase and Credit Facilities

CMBS – Term Repurchase Facility

In February 2011, the Company's wholly-owned subsidiaries, RCC Real Estate and RCC Commercial, entered into a master repurchase agreement with Wells Fargo Bank, National Association to be used as a warehouse facility to finance the purchase of CMBS. The Company guaranteed RCC Real Estate's and RCC Commercial's performance of their obligations under the repurchase agreement. At March 31, 2011, RCC Real Estate had borrowed \$15.1 million (gross of \$498,000 of deferred debt issuance costs), all of which the Company had guaranteed. At March 31, 2011,



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borrowings under the repurchase agreement were secured by CMBS with an estimated fair value of \$17.5 million and a weighted average interest rate of one-month LIBOR plus 1.25%, or 1.50% at March 31, 2011.

At March 31, 2011, the Company had repurchase agreements with the following counterparty (dollars in thousands); the Company had no repurchase agreements at December 31, 2010:

	Amount at Risk (1)	Weighted Average Maturity in Days	Weighted Average Interest Rate
March 31, 2011:			
Wells Fargo Bank, National Association.	\$ 3,056	18	1.50%

(1) Equal to the estimated fair value of securities or loans sold, plus accrued interest income, minus the sum of repurchase agreement liabilities plus accrued interest expense.

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RESOURCE CAPITAL CORP. AND SUBSIDIARIES  
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## NOTE 10 – SHARE ISSUANCE AND REPURCHASE

On March 30, 2011, the Company sold 6,900,000 shares of common stock in an underwritten public common stock follow-on offering, including 900,000 shares exercised through the underwriters' over-allotment option, at a price of \$6.90 per share. The Company received net proceeds of approximately \$46.6 million after payment of underwriting discounts and commissions of approximately \$966,000 and before other offering expenses of approximately \$185,000.

Under a dividend reinvestment plan authorized by the board of directors on November 18, 2010, the Company is authorized to issue up to 8.0 million shares of common stock. The Company issued 4.3 million shares of common stock under the plan during the three months ended March 31, 2011 at a weighted-average share price of \$7.18 per share and received proceeds of \$30.2 million (net of costs). The Company has issued a total of 5.7 million shares of common stock under the plan as of March 31, 2011.

## NOTE 11 – SHARE-BASED COMPENSATION

The following table summarizes restricted common stock transactions:

	Non-Employee		Total
	Directors	Non-Employees	
Unvested shares as of January 1, 2011	16,939	518,018	534,957
Issued	15,200	911,165	926,365
Vested	(16,939 )	(285,508 )	(302,447 )
Forfeited	–	–	–
Unvested shares as of March 31, 2011	15,200	1,143,675	1,158,875

The Company is required to value any unvested shares of restricted common stock granted to non-employees at the current market price. The estimated fair value of the unvested shares of restricted stock granted during the three months ended March 31, 2011 and 2010, including shares issued to the five non-employee directors, was \$6.7 million and \$1.8 million, respectively.

On January 26, 2011, the Company issued 316,480 shares of restricted common stock under its 2007 Omnibus Equity Compensation Plan. These restricted shares will vest in full on January 27, 2014.

On February 1, 2011 and March 8, 2011, the Company granted 3,120 and 12,080 shares of restricted stock, respectively, under its 2007 Omnibus Equity Compensation Plan, to the Company's non-employee directors as part of their annual compensation. These shares vest in full on the first anniversary of the date of grant.

On February 8, 2011, the Company issued 593,271 shares of restricted common stock under its 2007 Omnibus Equity Compensation Plan. Of this issuance, 69,156 of these restricted shares will vest on February 8, 2013 and the remaining 524,115 of these restricted shares will vest on February 10, 2014.

On February 23, 2011, the Company issued 1,414 shares of restricted common stock under its 2007 Omnibus Equity Compensation Plan. These shares will vest in full on February 24, 2014.



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## NOTE 11 – SHARE-BASED COMPENSATION – (Continued)

The following table summarizes stock option transactions:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding as of January 1, 2011	602,666	\$ 14.99		
Granted	–	–		
Exercised	–	–		
Forfeited	–	–		
Outstanding as of March 31, 2011	602,666	\$ 14.99	4	\$ 408
Exercisable at March 31, 2011	602,666	\$ 14.99	4	\$ 408

The stock options have a remaining contractual term of four years. Upon exercise of options, new shares are issued.

All of the Company's 602,666 stock options were vested as of March 31, 2011.

For the three months ended March 31, 2011 and 2010, the components of equity compensation expense were as follows (in thousands):

	Three Month Ended March 31,	
	2011	2010
Options granted to Manager and non-employees	\$–	\$20
Restricted shares granted to Manager and non-employees	432	676
Restricted shares granted to non-employee directors	28	28
Total equity compensation expense	\$460	\$724

During the three months ended March 31, 2011 and 2010, the Manager received 4,482 and 73,815 shares as incentive compensation valued at \$33,000 and \$375,000, respectively pursuant to the Management Agreement. The incentive management fee is paid one quarter in arrears.

Apart from incentive compensation payable under the Management Agreement, the Company has established no formal criteria for equity awards as of March 31, 2011. All awards are discretionary in nature and subject to approval by the compensation committee of the Company's board of directors.

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RESOURCE CAPITAL CORP. AND SUBSIDIARIES  
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## NOTE 12 – EARNINGS PER SHARE

The following table presents a reconciliation of basic and diluted earnings per share for the periods presented as follows (in thousands, except share and per share amounts):

	Three Months Ended March 31,	
	2011	2010
<b>Basic:</b>		
Net income	\$13,142	\$1,406
Weighted average number of shares outstanding	60,147,820	37,987,192
Basic net income per share	\$0.22	\$0.04
<b>Diluted:</b>		
Net income	\$13,142	\$1,406
Weighted average number of shares outstanding	60,147,820	37,987,192
Additional shares due to assumed conversion of dilutive instruments	249,810	163,413
Adjusted weighted-average number of common shares outstanding	60,397,630	38,150,605
Diluted net income per share	\$0.22	\$0.04

## NOTE 13 – RELATED PARTY TRANSACTIONS

## Relationship with Resource America and Certain of its Subsidiaries

At March 31, 2011, Resource America owned 2,448,484 shares, or 3.5%, of the Company's outstanding common stock. In addition, Resource America held 2,166 options to purchase restricted stock.

The Company is managed by the Manager pursuant to a management agreement that provides for both base and incentive management fees. For the three months ended March 31, 2011 and 2010, the Manager earned base management fees of approximately \$1.6 million and \$1.2 million, respectively. The Company also reimburses the Manager and Resource America for expenses and employees of Resource America who perform legal, accounting, due diligence and other services that outside professionals or consultants would otherwise perform. On October 16, 2009, the Company entered into an amendment to the management agreement. Pursuant to the amendment, the Manager must provide the Company with a Chief Financial Officer and three accounting professionals, each of whom will be exclusively dedicated to the operations of the Company. The Manager must also provide the Company with a director of investor relations who will be 50% dedicated to the Company's operations. The Company bears the expense of the wages, salaries and benefits of the Chief Financial Officer and three accounting professionals and 50% of the salary and benefits of the director of investor relations. In addition, in February 2010, the Company began reimbursing the Manager for the wages, salary, and benefits of its Chairman of the Board, who is exclusively dedicated to the operations of the Company. For the three months ended March 31, 2011 and 2010, the Company paid the Manager \$564,000 and \$440,000, respectively, as expense reimbursements.

At March 31, 2011, the Company was indebted to the Manager for base management fees of \$588,000 and expense reimbursements of \$246,000. At December 31, 2010, the Company was indebted to the Manager for base

management fees of \$522,000, incentive management fees of \$131,000 and expense reimbursements of \$256,000.

The Company purchased a membership interest in RRE VIP Borrower, LLC (an unconsolidated VIE that holds the Company's interests in a real estate joint venture) from Resource America at book value. This joint venture, which is structured as a credit facility with Värde Investment Partners, LP acting as lender, finances the acquisition of distressed properties and mortgage loans and has the objective of repositioning both the directly-owned properties and the properties underlying the mortgage loans to enhance their value. The Company acquired the membership interests for \$2.1 million. The agreement requires the Company to contribute 3% to 5% (depending on the asset agreement) of the total funding required for each asset acquisition on a monthly basis. The investment balance of \$5.2 million and \$5.2 million at March 31, 2011 and December 31, 2010, respectively, is recorded as an investment in unconsolidated entities on the Company's consolidated balance sheet using the equity method.

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NOTE 13 – RELATED PARTY TRANSACTIONS – (Continued)

Relationship with Resource America and Certain of its Subsidiaries – (Continued)

On January 15, 2010, the Company loaned \$2.0 million to Resource Capital Partners, Inc. (“RCP”), a wholly-owned subsidiary of the manager, so that it could acquire a 5.0% limited partnership interest in Resource Real Estate Opportunity Fund, L.P. (“RRE Opportunity Fund”). RCP is the general partner of the RRE Opportunity Fund. The loan is secured by RCP’s partnership interest in the RRE Opportunity Fund. The promissory note bears interest at a fixed rate of 8.0% per annum on the unpaid principal balance. In the event of default, interest will accrue and be payable at a rate of 5.0% in excess of the fixed rate. Interest is payable quarterly. Mandatory principal payments must also be made to the extent distributable cash or other proceeds from the partnership represents a return of RCP’s capital. The loan matures on January 14, 2015, with RCP, Inc. having options to extend the loan for two additional 12-month periods each.

On November 24, 2010, the Company entered into an Investment Management Agreement with Resource Capital Markets, Inc. (“RCM”), a wholly-owned subsidiary of Resource America. The agreement provides that: (a) RCM may invest up to \$13.0 million, with the investable amount being adjusted by portfolio gains/(losses) and collections, and offset by expenses, taxes and realized management fees, and (b) RCM can earn a management fee in any year that the net profits earned exceed a preferred return. The management fee is 20% of the amount by which the net profits exceed the preferred return. During the three months ended March 31, 2011, RCM earned \$530,000 in management fees. The Company has reinvested gains from its activity and holds \$31.3 million in fair market value of trading securities as of March 31, 2011, an increase from \$17.7 million at fair market value as of December 31, 2010. In addition, the Company and RCM have established an escrow account that allocates the net profit or net losses of the portfolio on a yearly basis based on the net asset value of the account. During the three months ended March 31, 2011, RCM earned \$118,000 as its share of the net profits as defined in the Investment Management Agreement.

Relationship with LEAF

On January 4, 2011, the Company’s wholly-owned subsidiary, Resource TRS, made a preferred investment in LCC, a newly-formed equipment financing subsidiary of LEAF Financial, a subsidiary of Resource America. Resource TRS contributed capital of approximately \$26.2 million to LCC in the form of approximately \$5.2 million in cash and \$21.0 million of directly-owned lease receivables, and all of Resource TRS’s interest in LEAF Receivables Funding 3, LLC, a wholly-owned subsidiary of Resource TRS. As part of the transaction, LEAF Financial contributed its assets relating to its equipment lease and note origination, servicing and finance business to LCC. Also, senior management personnel of LEAF Financial (collectively, the “Management Parties”), contributed capital to LCC in the form of all of the shares of common stock they owned in LEAF Financial in exchange for 10% of the shares of LCC common stock on a fully-diluted basis. The foregoing capital investments in LCC were made pursuant to a Transfer and Contribution Agreement among the registrant, LEAF Financial, LCC, Resource TRS and the Management Parties (the “TCA”).

Pursuant to the TCA, in return for TRS’s capital investments, LCC issued and delivered to Resource TRS 2,626,783 shares of LCC Series A preferred stock and warrants to purchase 4,800 shares of LCC common stock for an exercise price of \$0.01 per share, representing 48% of LCC’s common stock on a fully-diluted basis, classified as securities available-for-sale on the Company’s consolidated balance sheet.

As set forth in the TCA, on January 4, 2011, Resource TRS also delivered to LCC a Share Purchase Agreement under which LCC is permitted to require Resource TRS to purchase up to an additional \$10.0 million of Preferred Stock on the terms set forth therein, of which \$5.0 million was purchased during the period ended March 31, 2011.



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NOTE 13 – RELATED PARTY TRANSACTIONS – (Continued)

On May 27, 2010, the Company closed a \$120.0 million securitization adding to the Company's existing lease receivables. The securitization, LEAF Funding 3 (referred to above), issued equipment-backed securitized notes at a weighted average discounted price of 93.6%. At closing, \$14.4 million of proceeds were placed into a restricted account. The Company had \$21.0 million of equity invested in LEAF Funding 3 as of December 31, 2010. As of March 31, 2011, as described above, the Company had contributed its interest in LEAF Funding 3 to LCC.

On March 5, 2010, the Company entered into agreements with Lease Equity Appreciation Fund II, L.P. ("LEAF II"), pursuant to which the Company provided an \$8.0 million credit facility to LEAF II, of which all \$8.0 million was funded as of March 31, 2010. The credit facility had a one year term at 12% per year, payable quarterly, and was secured by all the assets of LEAF II Receivables Funding, LLC ("LEAF Funding II"), including its entire ownership interest in LEAF Funding II. The Company received a 1% origination fee in connection with the establishment of the facility. The facility originally matured on March 3, 2011 and was extended until June 3, 2011 with a 1% extension fee paid on the current outstanding loan balance. The loan amount outstanding at March 31, 2011 was \$8.0 million.

Relationship with Apidos Capital Management

Apidos Capital Management LLC ("ACM"), a subsidiary of Resource America, manages internally and externally originated bank loan assets on the Company's behalf. On February 24, 2011, the Company announced that it had entered into a definitive agreement that will expand its management in broadly syndicated bank loans. A subsidiary of the Company agreed to purchase 100% of the ownership interests in Churchill Pacific Asset Management LLC ("CPAM") from Churchill Financial Holdings LLC ("Churchill") for \$22.5 million. Through CPAM, the Company will be entitled to collect senior, subordinated and incentive fees related to five Collateralized Loan Obligations ("CLOs") totaling approximately \$1.9 billion in assets managed by CPAM. CPAM will be assisted by ACM, in managing the five CLOs. CPAM has subsequently changed its name to Resource Capital Asset Management ("RCAM"). ACM will be entitled to 10% of all subordinated fees and 5% of the incentive fees received by RCAM. For the period from acquisition through March 31, 2011, ACM was paid \$179,000 from subordinated fees received.

Relationship with Resource Real Estate

Resource Real Estate, a subsidiary of Resource America, originates, finances and manages the Company's commercial real estate loan portfolio, including whole loans, A notes, B notes and mezzanine loans. The Company reimburses Resource Real Estate for loan origination costs associated with all loans originated. At March 31, 2011 and December 31, 2010, the Company had no indebtedness to Resource Real Estate for loan origination costs in connection with the Company's commercial real estate loan portfolio.

Relationship with Law Firm

Until 1996, Edward E. Cohen, a director who was the Company's Chairman from its inception until November 2009, was of counsel to Ledgewood, P.C., a law firm. In addition, one of the Company's executive officers, Jeffrey F. Brotman, was employed by Ledgewood until 2007. Mr. Cohen receives certain debt service payments from Ledgewood related to the termination of his affiliation with Ledgewood and its redemption of his interest in the firm. Mr. Brotman also receives certain debt service payments from Ledgewood related to the termination of his affiliation

with the firm. For the three months ended March 31, 2011 and 2010, the Company paid Ledgewood \$49,000 and \$24,000, respectively, in connection with legal services rendered to the Company.

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RESOURCE CAPITAL CORP. AND SUBSIDIARIES  
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NOTE 14 – DISTRIBUTIONS

In order to qualify as a REIT, the Company must currently distribute at least 90% of its taxable income. In addition, the Company must distribute 100% of its taxable income in order not to be subject to corporate federal income taxes on retained income. The Company anticipates it will distribute substantially all of its taxable income to its stockholders. Because taxable income differs from cash flow from operations due to non-cash revenues or expenses (such as provisions for loan and lease losses and depreciation), in certain circumstances, the Company may generate operating cash flow in excess of its distributions or, alternatively, may be required to borrow to make sufficient distribution payments.

The Company's 2011 dividends will be determined by the Company's board of directors which will also consider the composition of any dividends declared, including the option of paying a portion in cash and the balance in additional common shares. Generally, dividends payable in stock are not treated as dividends for purposes of the deduction for dividends, or as taxable dividends to the recipient. However, the Internal Revenue Service, in Revenue Procedures 2009-15 and 2010-12, has given guidance with respect to certain stock distributions by publicly traded REITs. These Revenue Procedures apply to distributions made on or after January 1, 2008 and declared with respect to a taxable year ending on or before December 31, 2011. They provide that publicly-traded REITs can distribute stock to satisfy their REIT distribution requirements if stated conditions are met. These conditions include that at least 10% of the aggregate declared distributions be paid in cash and the shareholders be permitted to elect whether to receive cash or stock, subject to the limit set by the REIT on the cash to be distributed in the aggregate to all shareholders. The Company did not use these Revenue Procedures with respect to any distributions for its 2009 and 2010 taxable years, but may do so for distributions with respect to 2011.

On March 18, 2011, the Company declared a quarterly distribution of \$0.25 per share of common stock, \$17.6 million in the aggregate, which was paid on April 28, 2011 to stockholders of record on March 31, 2011.

NOTE 15 – FAIR VALUE OF FINANCIAL INSTRUMENTS

In analyzing the fair value of its investments accounted for on a fair value basis, the Company follows the fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The Company determines fair value based on quoted prices when available or, if quoted prices are not available, through the use of alternative approaches, such as discounting the expected cash flows using market interest rates commensurate with the credit quality and duration of the investment. The hierarchy followed defines three levels of inputs that may be used to measure fair value:

Level 1 - Quoted prices in active markets for identical assets and liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset and liability or can be corroborated with observable market data for substantially the entire contractual term of the asset or liability.

Level 3 - Unobservable inputs that reflect the entity's own assumptions about the assumptions that market participants would use in the pricing of the asset or liability and are consequently not based on market activity, but rather through particular valuation techniques.

The determination of where an asset or liability falls in the hierarchy requires significant judgment. The Company evaluates its hierarchy disclosures each quarter; depending on various factors, it is possible that an asset or liability may be classified differently from quarter to quarter. However, the Company expects that changes in classifications between levels will be rare.

Certain assets and liabilities are measured at fair value on a recurring basis. The following is a discussion of these assets and liabilities as well as the valuation techniques applied to each for fair value measurement.

The Company reports its investment securities available-for-sale at fair value. To determine fair value, the Company uses two methods, either a dealer quote or an internal valuation model, depending upon the current level of market activity.

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RESOURCE CAPITAL CORP. AND SUBSIDIARIES  
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NOTE 15 – FAIR VALUE OF FINANCIAL INSTRUMENTS – (Continued)

For securities purchased with higher levels of market activity, the Company obtains a quote from a dealer, which typically will be the dealer who sold the Company the security. The Company has been advised that, in formulating their quotes, dealers may use recent trades in the particular security, if any, market activity in similar securities, if any, or internal valuation models. These quotes are non-binding. As a result of how the dealers develop their quotes, the market illiquidity and low levels of trading activity in the past, the Company had categorized all of these investment securities available-for-sale in Level 3 in the fair value hierarchy. Due to the increased level of trading activity in 2010 and 2011, the Company moved some of these securities into Level 2 in the fair value hierarchy at September 30, 2010 and March 31, 2011. The Company evaluates the reasonableness of the quotes it receives by applying its own valuation models. If there is a material difference between a quote the Company receives and the value indicated by its valuation models, the Company will evaluate the difference. As part of that evaluation, the Company will discuss the difference with the dealer, who may revise their quote based upon these discussions. Alternatively, the Company may revise its valuation models.

For investment securities available-for-sale with lower levels of market activity, the Company determines fair value based on taking a weighted average of the following three measures:

dealer quotes, as described above;

quotes on more actively-traded, higher-rated securities issued in a similar time period, adjusted for differences in rating and seniority; and

the value resulting from an internal valuation model using an income approach based upon an appropriate risk-adjusted yield, time value and projected losses using default assumptions based upon an historical analysis of underlying loan performance.

The Company reports its investment securities, trading at fair value, which is based on a dealer quotes or bids which are validated using an income approach utilizing appropriate prepayment, default and recovery rates. Any changes in fair value are recorded on the Company's results of operations as net unrealized gain on investment securities, trading.

Derivatives (interest rate swaps and interest rate caps), both assets and liabilities, are reported at fair value, and are valued by a third-party pricing agent using an income approach with models that use, as their primary inputs, readily observable market parameters. This valuation process considers factors including interest rate yield curves, time value, credit factors and volatility factors. Although the Company has determined that the majority of the inputs used to value its derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives utilize Level 3 inputs, such as estimates of current credit spreads, to evaluate the likelihood of default by the Company and its counterparties. The Company has assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and has determined that the credit valuation adjustments have become significant to the overall valuation of some of its derivatives. As a result, the Company transferred derivatives with credit valuation adjustments to Level 3 in the fair value hierarchy from Level 2 in the fair value hierarchy as of December 31, 2010.



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RESOURCE CAPITAL CORP. AND SUBSIDIARIES  
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## NOTE 15 – FAIR VALUE OF FINANCIAL INSTRUMENTS – (Continued)

The following table presents information about the Company's assets (including derivatives that are presented net) measured at fair value on a recurring basis and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value as follows (in thousands):

	Level 1	Level 2	Level 3	Total
<b>March 31, 2011:</b>				
<b>Assets:</b>				
Investment securities, trading	\$–	\$–	\$31,270	\$31,270
Investment securities available-for-sale	–	66,345	24,744	91,089 (1)
<b>Total assets at fair value</b>	<b>\$–</b>	<b>\$66,345</b>	<b>\$56,014</b>	<b>\$122,359</b>
<b>Liabilities:</b>				
Derivatives (net)	\$–	\$1,930	\$10,079	\$12,009
<b>Total liabilities at fair value</b>	<b>\$–</b>	<b>\$1,930</b>	<b>\$10,079</b>	<b>\$12,009</b>
<b>December 31, 2010:</b>				
<b>Assets:</b>				
Investment securities, trading	\$–	\$–	\$17,723	\$17,723
Investment securities available-for-sale	–	38,303	25,657	63,960
<b>Total assets at fair value</b>	<b>\$–</b>	<b>\$38,303</b>	<b>\$43,380</b>	<b>\$81,683</b>
<b>Liabilities:</b>				
Derivatives (net)	\$–	\$2,363	\$10,929	\$13,292
<b>Total liabilities at fair value</b>	<b>\$–</b>	<b>\$2,363</b>	<b>\$10,929</b>	<b>\$13,292</b>

(1) Balance does not include a \$31.2 million investment in preferred stock and warrants which is carried at cost and therefore not required to be at fair value.

The following table presents additional information about assets which are measured at fair value on a recurring basis for which the Company has utilized Level 3 inputs (in thousands):

	Level 3
Beginning balance, January 1, 2010	\$ 44,542
<b>Total gains or losses (realized/unrealized):</b>	
Included in earnings	(6,936 )
Purchases	40,415
Sales	(19,468 )
Paydowns	(1,276 )
Transfers out of Level 3	(43,090 )
Unrealized losses – included in accumulated other comprehensive income	29,193
<b>Beginning balance, January 1, 2011</b>	<b>43,380</b>

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Total gains or losses (realized/unrealized):	
Included in earnings	2,347
Purchases	17,947
Sales	(6,043 )
Paydowns	(1,306 )
Transfers out of Level 3	(4,437 )
Unrealized losses – included in accumulated other comprehensive income	4,126
Ending balance, March 31, 2011	\$ 56,014



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RESOURCE CAPITAL CORP. AND SUBSIDIARIES  
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## NOTE 15 – FAIR VALUE OF FINANCIAL INSTRUMENTS – (Continued)

The following table presents additional information about liabilities which are measured at fair value on a recurring basis for which the Company has utilized Level 3 inputs (in thousands):

	Level 3
Beginning balance, January 1, 2010	\$ –
Transfers into Level 3	10,929
Beginning balance, January 1, 2011	10,929
Unrealized losses – included in accumulated other comprehensive income	850
Ending balance, March 31, 2011	\$ 10,079

The Company did not have any losses included in earnings due to other-than-temporary impairment charges during the three months ended March 31, 2011 and 2010.

Loans held for sale consist of bank loans and commercial real estate loans (“CRE loans”) identified for sale due to credit concerns. Interest on loans held for sale is recognized according to the contractual terms of the loan and included in interest income on loans. The fair value of bank loans held for sale and impaired bank loans is based on what secondary markets are currently offering for these loans. As such, the Company classifies these loans as recurring Level 2. For the Company’s CRE loans where there is no market, fair value is measured using discounted cash flow analysis and other valuation techniques and these loans are classified as nonrecurring Level 3. The amount of nonrecurring fair value losses for impaired loans for the three months ended March 31, 2011 and 2010 was \$3.4 million and \$15.1 million, respectively, and is included in the consolidated statements of income as provision for loan and lease losses.

Property available-for-sale is estimated based on recent sales prices of prior similar condominium units in the property and the appraised value of a similar condominium unit in the property less costs to sell

The following table summarizes the financial assets and liabilities measured at fair value on a nonrecurring basis and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value as follows (in thousands):

	Level 1	Level 2	Level 3	Total
<b>March 31, 2011:</b>				
Assets:				
Loans held for sale	–	9,890	32,954	42,844
Total assets at fair value	\$–	\$9,890	\$32,954	\$42,844
<b>December 31, 2010:</b>				
Assets:				
Loans held for sale	\$–	\$4,027	\$24,566	\$28,593
Impaired loans	–	250	132,777	133,027
Property available-for-sale	–	–	4,444	4,444
Equity	–	–	147	147
Total assets at fair value	\$–	\$4,277	\$161,934	\$166,211



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RESOURCE CAPITAL CORP. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)  
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## NOTE 15 – FAIR VALUE OF FINANCIAL INSTRUMENTS – (Continued)

The Company is required to disclose the fair value of financial instruments for which it is practicable to estimate that value. The fair value of short-term financial instruments such as cash and cash equivalents, restricted cash, dividend reinvestment plan proceeds receivable, interest receivable, distribution payable and accrued interest expense approximates their carrying value on the consolidated balance sheet. The fair value of the Company's investment securities, trading is reported in Note 4. The fair value of the Company's investment securities available-for-sale is reported in Note 5. The fair value of the Company's investment securities held-to-maturity is reported in Note 6. The fair value of the Company's derivative instruments is reported in Note 16.

The fair values of the Company's remaining financial instruments that are not reported at fair value on the consolidated balance sheet are reported below.

	Fair Value of Financial Instruments (in thousands)			
	March 31, 2011		December 31, 2010	
	Carrying value	Fair value	Carrying value	Fair value
Loans held-for-investment	\$ 1,435,945	\$ 1,436,290	\$ 1,443,271	\$ 1,439,376
Loans receivable-related party	\$ 9,689	\$ 9,689	\$ 9,927	\$ 9,927
CDOs	\$ 1,398,653	\$ 1,054,269	\$ 1,397,880	\$ 905,790
Junior subordinated notes	\$ 50,431	\$ 16,924	\$ 50,354	\$ 16,848

## NOTE 16– INTEREST RATE RISK AND DERIVATIVE INSTRUMENTS

At March 31, 2011, the Company had 18 interest rate swap contracts outstanding whereby the Company paid an average fixed rate of 4.75% and received a variable rate equal to one-month LIBOR. The aggregate notional amount of these contracts was \$186.1 million at March 31, 2011. In addition, the Company also has one interest rate cap agreement with an aggregate notional amount of \$14.8 million outstanding whereby it reduced its exposure to variability in future cash flows attributable to LIBOR. The interest rate cap is a non-designated cash flow hedge and, as a result, the change in fair value is recorded through the consolidated statements of income. The counterparties for the Company's designated interest rate hedge contracts are Credit Suisse International and Wells Fargo Bank, National Association, with which the Company has master netting agreements.

At December 31, 2010, the Company had 10 interest rate swap contracts outstanding whereby the Company paid an average fixed rate of 5.17% and received a variable rate equal to one-month LIBOR. The aggregate notional amount of these contracts was \$166.8 million at December 31, 2010. In addition, the Company also has one interest rate cap agreement with an aggregate notional amount of \$14.8 million outstanding, as described above.

The estimated fair value of the Company's interest rate swaps was (\$12.0) million and (\$13.3) million as of March 31, 2011 and December 31, 2010, respectively. The Company had aggregate unrealized losses of \$13.3 million and \$14.7 million on the interest rate swap agreements as of March 31, 2011 and December 31, 2010, respectively, which is recorded in accumulated other comprehensive loss. In connection with the August 2006 close of RREF CDO 2006-1, the Company realized a swap termination loss of \$119,000, which is being amortized over the term of RREF CDO

2006-1. The amortization is reflected in interest expense in the Company's consolidated statements of income. In connection with the June 2007 close of RREF CDO 2007-1, the Company realized a swap termination gain of \$2.6 million, which is being amortized over the term of RREF CDO 2007-1. The accretion is reflected in interest expense in the Company's consolidated statements of income. In connection with the termination of a \$53.6 million swap related to RREF CDO 2006-1 during the nine months ended September 30, 2008, the Company realized a swap termination loss of \$4.2 million, which is being amortized over the term of a new \$45.0 million swap. The amortization is reflected in interest expense in the Company's consolidated statements of income. In connection with the payoff of a fixed-rate commercial real estate loan during the three months ended September 30, 2008, the Company terminated a \$12.7 million swap and realized a \$574,000 swap termination loss, which is being amortized over the term of the terminated swap. The amortization is reflected in interest expense in the Company's consolidated statements of income.

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RESOURCE CAPITAL CORP. AND SUBSIDIARIES  
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## NOTE 16– INTEREST RATE RISK AND DERIVATIVE INSTRUMENTS – (Continued)

The following tables present the fair value of the Company's derivative financial instruments as well as their classification on the balance sheet as of March 31, 2011 and on the consolidated statement of operations for the three months ended March 31, 2011:

Fair Value of Derivative Instruments as of March 31, 2011  
(in thousands)

	Notional Amount	Liability Derivatives	
		Balance Sheet Location	Fair Value
Interest rate cap agreement	\$ 14,841	Derivatives, at fair value	\$ –
Interest rate swap contracts	\$ 186,119	Derivatives, at fair value	\$ (12,009 )
		Accumulated other comprehensive loss	\$ 12,009

The Effect of Derivative Instruments on the Statement of Operations for the  
For the Three Months Ended March 31, 2011  
(in thousands)

	Notional Amount	Liability Derivatives	
		Statement of Operations Location	Unrealized Loss (1)
Interest rate cap agreement	\$ 14,841	Interest expense	\$ –
Interest rate swap contracts	\$ 186,119	Interest expense	\$ 2,114

(1) Negative values indicate a decrease to the associated balance sheet or consolidated statement of operations line items.

## NOTE 17 – SUBSEQUENT EVENTS

The Company has evaluated subsequent events through the filing of this form and determined that there have not been any events that have occurred that would require adjustments to or disclosures in the unaudited consolidated financial statements, other than listed below.

On May 2, 2011, the Company sold a mezzanine loan secured by an office portfolio with an amortized cost of \$19.5 million at par. There were transaction costs of approximately \$700,000 associated with the sale of this loan. This loan is classified as a loan held for sale on the consolidated balance sheet as of March 31, 2011.

On May 2, 2011, the Company sold a B-note secured by a hotel with an amortized cost of \$15.0 million for \$12.75 million and recorded a \$2.25 million provision for loan losses as of March 31, 2011, accordingly. This loan is classified as a loan held for sale on the consolidated balance sheet as of March 31, 2011.

The Company received \$5.6 million in proceeds related to the issuance of 899,648 shares of common stock on the Company's dividend reinvestment plan related to April 2011.

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## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion provides information to assist you in understanding our financial condition and results of operations. This discussion should be read in conjunction with our consolidated financial statements and related notes appearing elsewhere in this report. This discussion contains forward-looking statements. Actual results could differ materially from those expressed in or implied by those forward-looking statements. Please see "Forward-Looking Statements" and "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2010 for a discussion of certain risks, uncertainties and assumptions associated with those statements.

### Overview

We are a specialty finance company that focuses primarily on commercial real estate and commercial finance. We are organized and conduct our operations to qualify as a REIT under Subchapter M of the Internal Revenue Code of 1986, as amended. Our objective is to provide our stockholders with total returns over time, including quarterly distributions and capital appreciation, while seeking to manage the risks associated with our investment strategy. We invest in a combination of real estate-related assets and, to a lesser extent, higher-yielding commercial finance assets. We have financed a substantial portion of our portfolio investments through borrowing strategies seeking to match the maturities and repricing dates of our financings with the maturities and repricing dates of those investments, and have sought to mitigate interest rate risk through derivative instruments.

We are externally managed by Resource Capital Manager, Inc., a wholly-owned indirect subsidiary of Resource America, Inc. (NASDAQ: REXI), or Resource America, a specialized asset management company that uses industry-specific expertise to evaluate, originate, service and manage investment opportunities through its commercial real estate, commercial finance and financial fund management operating segments. As of March 31, 2011, Resource America managed approximately \$13.7 billion of assets in these sectors. To provide its services, the Manager draws upon Resource America, its management team and their collective investment experience.

We generate our income primarily from the spread between the revenues we receive from our assets and the cost to finance the purchase of those assets and from hedging interest rate risks. We generate revenues from the interest and fees we earn on our whole loans, A notes, B notes, mezzanine debt, commercial mortgage-backed securities, or CMBS, bank loans, payments on lease receivables and other asset-backed securities, or ABS, and the management of externally originated bank loans. Historically, we have used a substantial amount of leverage to enhance our returns and we have financed each of our different asset classes with different degrees of leverage. The cost of borrowings to finance our investments is a significant part of our expenses. Our net income depends on our ability to control these expenses relative to our revenue. In our bank loans, CMBS, lease receivables and other ABS, we historically have used warehouse facilities as a short-term financing source and collateralized debt obligations, or CDOs, and, to a lesser extent, other term financing as long-term financing sources. In our commercial real estate loan portfolio, we historically have used repurchase agreements as a short-term financing source, CDOs and, to a lesser extent, other term financing as long-term financing sources. Our other term financing has consisted of long-term match-funded financing provided through long-term bank financing and asset-backed financing programs, depending upon market conditions and credit availability.

Ongoing problems in commercial real estate and credit markets continue to impact our operations, particularly with respect to our legacy real estate portfolio investments made in the 2005 to 2008 timeframe that are still held by us. We refer to these investments as our legacy portfolio investments. These problems have also affected a number of our commercial real estate borrowers and, with respect to 27 of our commercial real estate loans, caused us to enter into loan modifications. We have increased our allowance for loan and lease losses to reflect the effect of these conditions

on our borrowers and have recorded both temporary and other-than-temporary impairments in the market valuation of the CMBS and other ABS in our investment portfolio. While we believe we have appropriately valued the assets in our investment portfolio at March 31, 2011, we cannot assure you that further impairments will not occur or that our assets will otherwise not be adversely affected by market conditions.

The events occurring in the credit markets have impacted our financing and investing strategies and, as a result, our ability to originate new investments and to grow. The market for securities issued by new securitizations collateralized by assets similar to those in our investment portfolio had largely disappeared until mid 2010. During 2010, we began to see a loosening in the previously frozen credit markets and in May 2010, we closed a new \$120.0 million securitization on our equipment leasing portfolio. In addition, in February 2011, we entered into a \$100.0 million, two-year term facility with Wells Fargo Bank, National Association, to purchase CMBS. In 2011, we have begun discussions with multiple potential lenders about providing commercial real estate term financing to augment our loan origination platform. However, we caution investors that even if credit through these markets becomes more available, we may be unable to access those markets on economically favorable terms, or at all.



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Credit market and economic conditions during the past three years also have resulted in a significant number of loan modifications, particularly in our commercial real estate, or CRE loans. Borrowers have experienced deterioration in the performance of the properties we have financed or delays in implementing their business plans. In order to assist our borrowers in effectuating their business plans, including the leasing and repositioning of the underlying assets, we have been willing to enter into loan modifications that would adapt our financing to their particular situations. The most common loan modifications have included term extensions and modest interest rate reductions through the lowering of London Interbank Offered Rate, or LIBOR, floors, offset by increased interest rate spreads over LIBOR. In exchange for the loan modifications, we have received partial principal pay-downs, new equity investment commitments in the properties from the borrowers or their principals, additional fees and other structural improvements and credit enhancements to the loans. Since the beginning of 2008 through March 31, 2011, we have modified 27 commercial real estate, or CRE, loans. Management determined that nine of these modifications was due to financial distress of the borrower and, accordingly, qualified as a troubled debt restructuring. We expect that we may have more CRE loan modifications in the future.

As economic conditions improve, and until we are able to access the credit markets on acceptable terms, our principal strategies are to manage our liquidity and originate new assets primarily through capital recycling as loan payoffs and paydowns occur and through existing capacities within our completed securitizations. The following is a summary of repayments we received on our consolidated CDOs during the three months ended March 31, 2011:

\$1.9 million of commercial real estate loan principal repayments;

\$24.6 million at commercial real estate loan sale proceeds;

\$142.0 million of bank loan principal repayments; and

\$9.1 million of bank loan sale proceeds.

We have used recycled capital in our CRE CDO and bank loan CDO structures to make new investments at discounts to par. As a result of the reinvested capital at discounts, the new investments will produce additional income as the discounts are accreted through interest income. From the net discounts of approximately \$15.3 million and \$25.8 million, we expect to recognize income of approximately \$4.1 million and \$14.6 million in our CRE CDO and bank loan CDO portfolio, respectively, in 2011.

During 2010, we invested \$5.0 million through Resource TRS, Inc. or Resource TRS, our taxable REIT subsidiary, in structured finance vehicles, principally CDO equity, which we have classified as trading securities. Because of the success of that new investment, we have committed an additional \$8.0 million in the March 2011 quarter. Beginning in October 2010 through April 2011, we have underwritten five new CRE loans for a total of \$40.2 million. We also purchased seven newly underwritten CMBS for \$22.8 million in the three months ended March 31, 2011 in conjunction with the Wells Fargo facility. Furthermore, in January 2011, we discontinued directly investing in our lease receivable portfolio investments and, instead made a preferred stock investment in LEAF Commercial Capital, Inc, or LCC, a recently formed equipment leasing enterprise and a subsidiary of our Manager, through cash capital contributions and a contribution of our lease portfolio equity interests. In February 2011, we purchased a company that manages \$1.9 billion of bank loan assets and are entitled to collect senior, subordinated and incentive management fees. As a result of these recent asset purchases and credit market events, we believe that we will be able to invest a significant portion of our available unrestricted and restricted cash balances and, as a result, modestly increase our net interest margin in 2011.

As of March 31, 2011, we had invested 71% of our portfolio in CRE assets, 17% in commercial bank loans and bank loan management, 7% in our preferred equity investment in LCC and 5% in structured notes. As of December 31,

2010, we had invested 77% of our portfolio in CRE assets, 18% in commercial bank loans, 3% in lease receivables and 2% in structured notes.

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## Critical Accounting Policies

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of our assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to the provision for credit losses, recovery of deferred tax assets, fair value of investment securities, potential impairment of intangible assets and goodwill, guarantees and certain accrued liabilities. We base our estimates on historical experience and on various other assumptions that we believe reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

For a complete discussion of our critical accounting policies and estimates, see the discussion of our Annual Report on Form 10-K for the year ended December 31, 2010 under “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies and Estimates.”

## Results of Operations – Three Months Ended March 31, 2011 as compared to Three Months Ended March 31, 2010

Our net income for the three months ended March 31, 2011 was \$13.1 million, or \$0.22 per share (basic and diluted), as compared to net income of \$1.4 million, or \$0.04 per share (basic and diluted), for the three months ended March 31, 2010.

## Interest Income

The following tables set forth information relating to our interest income recognized for the periods presented (in thousands, except percentages):

	Three Months Ended March 31, 2011			Three Months Ended March 31, 2010		
	Interest Income	Weighted Average Yield	Balance	Interest Income	Weighted Average Yield	Balance
Interest income:						
Interest income from loans:						
Bank loans	\$ 13,048	5.91%	\$ 878,019	\$ 9,721	4.27%	\$ 907,934
Commercial real estate loans	7,100	4.28%	\$ 644,479	8,664	4.71%	\$ 727,131
Total interest income from loans	20,148			18,385		
Interest income from securities:						
CMBS-private placement	2,234	6.00%	\$ 148,578	2,534	7.53%	\$ 131,247
Securities held-to-maturity	370	4.64%	\$ 31,953	337	3.75%	\$ 35,945
Other ABS	–	N/A	N/A	3	N/A	N/A
Total interest income from securities available-for-sale	2,604			2,874		
Leasing	–	N/A	N/A	235	10.50%	\$ 9,164

## Interest income – other:

Preference payments on structured notes	1,291	N/A	N/A	–	N/A	N/A
Temporary investment in over-night repurchase agreements	1,186	N/A	N/A	215	N/A	N/A
Total interest income – other	2,477			215		
Total interest income	\$ 25,229			\$ 21,709		

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The following table summarizes certain information relating to interest income for the periods indicated (in thousands, except percentages):

Type of Security	Coupon Interest	Unamortized (Discount) Premium	Net Amortization/ Accretion	Interest Income	Fee Income	Total
<b>Three Months Ended March 31, 2011:</b>						
Bank loans	3.61%	\$ (23,089 )	\$ 5,052	\$ 7,996	\$ –	\$ 13,048
Commercial real estate loans	4.34%	\$ (173 )	(2 )	7,057	45	7,100
Total interest income from loans			5,050	15,053	45	20,148
CMBS-private placement	3.27%	\$ (19,693 )	1,016	1,218	–	2,234
Securities held-to-maturity	2.63%	\$ (2,726 )	118	252	–	370
Other ABS			–	–	–	–
Total interest income from securities			1,134	1,470	–	2,604
Preference payments on structured notes			–	1,291	–	1,291
Other			–	1,186	–	1,186
Total interest income – other			–	2,477	–	2,477
Total interest income			\$ 6,184	\$ 19,000	\$ 45	\$ 25,229
<b>Three Months Ended March 31, 2010:</b>						
Bank loans	3.00%	\$ (29,864 )	\$ 2,873	\$ 6,848	\$ –	\$ 9,721
Commercial real estate loans	4.84%	\$ (36 )	(6 )	8,557	113	8,664
Total interest income from loans			2,867	15,405	113	18,385
CMBS-private placement	4.24%	\$ (30,807 )	1,080	1,454	–	2,534
Securities held-to-maturity	2.38%	\$ (2,981 )	97	240	–	337
Other ABS			–	3	–	3
Total interest income from securities			1,177	1,697	–	2,874
Leasing			–	235	–	235
Preference payments on structured notes			–	–	–	–
Other			–	215	–	215
Total interest income – other			–	215	–	215
Total interest income			\$ 4,044	\$ 17,552	\$ 113	\$ 21,709

Aggregate interest income increased \$3.5 million (16%) to \$25.2 million for the three months ended March 31, 2011 from \$21.7 million for the three months ended March 31, 2010. We attribute this increase to the following:

#### Interest Income from Loans

Aggregate interest income from loans increased \$1.7 million (10%) to \$20.1 million for the three months ended March 31, 2011 from \$18.4 million for the three months ended March 31, 2010.

Bank loans generated \$13.0 million of interest income for the three months ended March 31, 2011 as compared to \$9.7 million for the three months ended March 31, 2010, an increase of \$3.3 million (34%). This increase resulted primarily from an increase in the weighted average yield earned by our bank loans to 5.91% for the three months ended March 31, 2011 from 4.27% for the three months ended March 31, 2010. This was principally a result of an increase in accretion income to \$5.1 million for the three months ended March 31, 2011 as compared to \$2.9 million for the three months ended March 31, 2010. The increase in accretion income is the result of the purchase of \$608.8 million of bank loans at discounts during 2009 and 2010 and the subsequent paydown and payoff of many of these loans during the three months ended March 31, 2011 which speeds up the recognition of the discount accretion. In addition, the normal accretion of those discounts into income is greater due to the larger discounts at March 31, 2011 as compared to March 31, 2010. These discounted loan purchases are made as we reinvest the proceeds from loan payoffs from our borrowers and from the loans we have sold, typically for credit reasons.

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The increase in bank loan accretion income was partially offset by a decrease in the weighted average balance on these loans of \$29.9 million to \$878.0 million for the three months ended March 31, 2011, from \$907.9 million for the three months ended March 31, 2010, primarily as a result of the timing of when loans were sold or paid down and the proceeds reinvested.

The increase in interest income from bank loans was partially offset by a decrease in interest income on CRE loans which generated \$7.1 million of interest income for the three months ended March 31, 2011 as compared to \$8.7 million for the three months ended March 31, 2010, a decrease of \$1.6 million (18%). This decrease is a result of the following:

a decrease in the weighted average balance of assets of \$82.6 million to \$644.5 million for the three months ended March 31, 2011 from \$727.1 million for the three months ended March 31, 2010 primarily as a result of payoffs and paydowns and, to a lesser extent, loan sales and write-offs of impaired loans; and

a decrease in the weighted average yield on these assets to 4.28% for the three months ended March 31, 2011 from 4.71% for the three months ended March 31, 2010, primarily due to decreases in LIBOR floors, which is a reference index for the rates payable on these loans, from loan modifications during 2009 and 2010. There were \$150.6 million of loans with a weighted average LIBOR floor of 2.45% at March 31, 2011 as compared to \$189.6 million of loans with a weighted average LIBOR floor of 2.24% at March 31, 2010.

#### Interest Income from Securities

Aggregate interest income from securities available-for-sale decreased \$270,000 (9%) to \$2.6 million for the three months ended March 31, 2011 from \$2.9 million for the three months ended March 31, 2010. The decrease in interest income from securities available-for-sale resulted principally from CMBS-private placement which decreased \$300,000 (12%) to \$2.2 million for the three months ended March 31, 2011 as compared to \$2.5 million for the three months ended March 31, 2010. We attribute the decrease primarily to the decrease in the weighted average yield on these assets to 6.00% for the three months ended March 31, 2011 from 7.53% for the three months ended March 31, 2010 as a result of impairment of \$35.3 million of bonds during the year ended December 31, 2010 that had higher yields than the other performing positions. The decrease in weighted average rate was partially offset by an increase in weighted average balance of assets of \$17.3 million to \$148.6 million at March 31, 2011 from \$131.2 million at March 31, 2010 as a result of the purchase of \$22.5 million par value of assets, primarily financed through our new repurchase facility, during the three months ended March 31, 2011.

#### Interest Income – Leasing

Our equipment leasing portfolio generated \$235,000 of interest income for the three months ended March 31, 2010. There was no such income for the three months ended March 31, 2011 as a result the transfer of our leasing portfolio into LCC as a preferred equity investment by us. Our investment in LCC, however, generated dividend income, as discussed in “- Other Revenue.”

#### Interest Income – Other

Aggregate interest income-other increased \$2.3 million (1,052%) to \$2.5 million for the three months ended March 31, 2011 as compared to \$215,000 for the three months ended March 31, 2010. The preference payments on structured notes generated \$1.3 million for the three months ended March 31, 2011. These payments related to our program with Resource Capital Markets vary from period to period and are based on cash flows from the underlying assets rather than on a contractual interest rate. There was no such portfolio or income for the three months ended

March 31, 2010.

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Interest Expense – Three Months Ended March 31, 2011 as compared to Three Months Ended March 31, 2010

The following table sets forth information relating to our interest expense incurred for the periods presented by asset class (in thousands, except percentages):

	Three Months Ended March 31, 2011			Three Months Ended March 31, 2010		
	Interest Expense	Yield	Balance	Interest Expense	Yield	Balance
Bank loans	\$ 2,290	1.00%	\$ 906,000	\$ 2,193	0.97%	\$ 906,000
Commercial real estate loans	1,589	1.24%	\$ 507,362	2,113	1.43%	\$ 587,314
CMBS–private placement	56	6.27%	\$ 3,612	–	N/A	N/A
General	2,998	5.88%	\$ 217,064	3,631	5.5%7	\$ 256,048
Total interest expense	\$ 6,933			\$ 7,937		

Aggregate interest expense decreased \$1.0 million (13%) to \$6.9 million for the three months ended March 31, 2011 from \$7.9 million for the three months ended March 31, 2010. We attribute this decrease to the following:

Interest expense on commercial real estate loans was \$1.6 million for the three months ended March 31, 2011 as compared to \$2.1 million for the three months ended March 31, 2010, a decrease of \$524,000 (25%). This decrease resulted primarily from a decrease in the weighted average balance of the related financings of \$80.0 million to \$507.4 million for the three months ended March 31, 2011 as compared to \$587.4 million for the three months ended March 31, 2010, primarily due to the repurchase of \$91.4 million of notes in 2010.

General interest expense was \$3.0 million for the three months ended March 31, 2011 as compared to \$3.6 million for the three months ended March 31, 2010, a decrease of \$633,000 (17%). This decrease was primarily from a decrease in the notional amount of our interest rate swap portfolio as a result of maturities on previous commitments during 2010.

#### Other Revenue

The following table sets forth information relating to our other revenue incurred for the periods presented (in thousands):

	Three Months Ended March 31,	
	2011	2010
Other revenue:		
Dividend income	661	–
Fee income	1,646	–
Total other revenue	\$2,307	\$–

We received dividend income of \$661,000 for the three months ended March 31, 2011 from our January 2011 investment in LCC. There was no such investment at March 31, 2010.

We generated fee income of \$1.6 million for the three months ended March 31, 2011 which is related to our February 2011 acquisition of a company that manages bank loan assets that entitles us to collect senior, subordinated, and

incentive fees related to five collateralized loan obligation issuers, or CLOs. We had no such investment or income at March 31, 2010.

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## Non-Investment Expenses

The following table sets forth information relating to our non-investment expenses incurred for the periods presented (in thousands):

	Three Months Ended March 31,	
	2011	2010
Non-investment expenses:		
Management fees – related party	\$2,338	\$1,152
Equity compensation – related party	460	722
Professional services	919	819
Insurance	177	212
General and administrative	945	647
Amortization of intangible asset	253	–
Income tax expense	1,809	105
Total non-investment expenses	\$6,901	\$3,657

Management fees – related party increased \$1.2 million (103%) to \$2.3 million for the three months ended March 31, 2011 as compared to \$1.2 million for the three months ended March 31, 2010. These amounts represent compensation in the form of base management fees and incentive management fees pursuant to our management agreement as well as fees to the manager of our structured note portfolio. The base management fees increased by \$430,000 (37%) to \$1.6 million for the three months ended March 31, 2011 as compared to \$1.2 million for the three months ended March 31, 2010. This increase was due to increased stockholders' equity, a component in the formula by which base management fees are calculated, primarily as a result of the receipt of \$106.8 million of net proceeds from the sales of common stock through our Dividend Reinvestment and stock repurchase Plan or DRIP during the year ended December 31, 2010 and the three months ended March 31, 2011 as well as the receipt of \$92.9 million from the proceeds of our May 2010 and March 2011 common stock offerings. Management fees also include fees of \$756,000 for the three months ended March 31, 2011 related to our structured finance manager. There was no such portfolio or related fee for the three months ended March 31, 2010. There were no incentive management fees for the three months ended March 31, 2011 or 2010.

Equity compensation – related party decreased \$262,000 (36%) to \$460,000 for the three months ended March 31, 2011 as compared to \$722,000 for the three months ended March 31, 2010. These expenses relate to the amortization of annual grants of restricted common stock to our non-employee independent directors, and annual and discretionary grants of restricted stock to several employees of Resource America who provide investment management services to us through our Manager. The decrease in expense was primarily the result of a decrease in our stock price and its impact on our quarterly remeasurement of the value of unvested stock. The decrease in expense from remeasurement was partially offset by the issuance of new grants during the year.

Professional services increased \$100,000 (12%) to \$919,000 for the three months ended March 31, 2011 as compared to \$819,000 for the three months ended March 31, 2010 as a result of an increase of \$129,000 in legal fees primarily from general legal expense related to the CRE portfolio.

General and administrative expense increased \$298,000 (46%) to \$945,000 for the three months ended March 31, 2011 from \$647,000 for the three months ended March 31, 2010. This increase is a result of the following:

\$136,000 of real estate expenses from our acceptance of a portfolio of condominiums as a partial loan settlement in September 2010; and

\$81,000 of this increase is related to our agreement to reimburse Resource America for the wages, salary and benefits of our Chief Financial Officer, three accounting professionals, our Chairman and 50% of the salary and benefits of a director of investor relations. We began reimbursing for our Chairman in February 2010.

Income tax expense increased \$1.7 million (1,623%) to \$1.8 million for the three months ended March 31, 2011 as compared to \$105,000 for the three months ended March 31, 2010 primarily due to activity in our structured finance portfolio and fee income from our externally originated bank loan portfolio which both yielded significant pre-tax income in the 2011 period.

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## Other (Expense)/Income

The following table sets forth information relating to our other (expense) income incurred for the periods presented (in thousands):

	Three Months Ended March 31,	
	2011	2010
Impairment losses on investment securities	\$(665 )	\$(2,665 )
Recognized in other comprehensive loss	(665 )	(2,665 )
Net impairment losses recognized in earnings	–	–
Net realized gain on investment securities available-for-sale and loans	35	146
Net realized gain on investment securities, trading	2,263	–
Net unrealized loss on investment securities, trading	(336 )	–
Provision for loan and lease losses	(2,606 )	(15,371 )
Gain on the extinguishment of debt	–	6,628
Other income (expense)	84	(112 )
Total	\$(560 )	\$(8,709 )

Net realized and unrealized gains (losses) on investment securities, trading was a gain of \$2.3 million and a loss of \$336,000 for three months ended March 31, 2011, respectively. No such portfolio existed prior to June 2010. The gains are the result of sales of structured finance securities. The losses are the result of marking the structured finance securities to market at March 31, 2011.

Our provision for loan and lease losses decreased \$12.8 million (83%) to \$2.6 million for the three months ended March 31, 2011 as compared to \$15.4 million for the three months ended March 31, 2010.

The following table summarizes information relating to our provision for loan and lease losses for the periods presented (in thousands):

	Three Months Ended March 31,	
	2011	2010
CRE loan portfolio	\$3,121	\$15,500
Bank loan portfolio	(515 )	(215 )
Lease receivables	–	86
	\$2,606	\$15,371

The principal reason for the decrease from the three months ended March 31, 2010 was improvement in our CRE portfolio. We had three positions for which we took a provision during the three months ended March 31, 2010. The positions had a total par amount of \$48.5 million and were written down to \$34.0 million for a weighted average write-down percentage of 29.9% of par. For the three months ended March 31, 2011, we had three positions for which we took a provision. The positions had a total par of \$70.5 million with a weighted average write down percentage of 3.8% of par.

Gain on the extinguishment of debt was \$6.6 million for the three months ended March 31, 2010 and is due to the buyback of a portion of the debt issued by RREF 2006-1 and RREF 2007-1 during the period. The notes, issued at par, were bought back as an investment by us at a weighted average price of 67.3%. The related deferred debt issuance costs were immaterial. There was no such transaction in the three months ended March 31, 2011.

Other income (expense) increased \$196,000 to income of \$84,000 from an expense of \$112,000. This increase is primarily the result of an increase of \$161,000 on income from a real estate joint venture.

#### Financial Condition

##### Summary.

Our total assets at March 31, 2011 were \$1.9 billion virtually unchanged from December 31, 2010. As of March 31, 2011, we held \$61.5 million of unrestricted cash and cash equivalents.

##### Investment Portfolio.

The table below summarizes the amortized cost and net carrying amount of our investment portfolio as of March 31, 2011 and December 31, 2010, classified by interest rate type. The following table includes both (i) the amortized cost of our investment portfolio and the related fair value, which is computed by dividing amortized cost by par amount, and (ii) the net carrying amount of our investment portfolio and the related fair value, which is computed by dividing the net carrying amount by par amount (in thousands, except percentages):

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	Amortized cost (3)	Dollar price	Net carrying amount	Dollar price	Net carrying amount less amortized cost	Dollar price
March 31, 2011						
Floating rate						
CMBS-private placement	\$ 29,946	100.00%	\$ 10,328	34.49%	\$ (19,618 )	-65.51%
Structured notes	21,989	26.25%	31,270	37.33%	9,281	11.08%
Other ABS	–	–%	23	0.26%	23	0.26%
B notes (1)	11,492	99.93%	11,324	98.47%	(168 )	-1.46%
Mezzanine loans (1)	81,878	100.00%	80,679	98.54%	(1,199 )	-1.46%
Whole loans (1)	459,405	99.90%	437,906	95.23%	(21,499 )	-4.67%
Bank loans (2)	865,910	97.37%	866,541	97.44%	631	0.07%
Loans held for sale (3)	23,316	86.37%	23,316	86.37%	–	–%
ABS held-to-maturity (4)	29,206	91.46%	26,903	84.26%	(2,303 )	-7.20%
Total floating rate	1,523,142	93.82%	1,488,290	91.67%	(34,852 )	-2.15%
Fixed rate						
CMBS – private placement	75,532	58.45%	80,738	62.48%	5,206	4.03%
B notes (1)	30,925	99.51%	30,472	98.05%	(453 )	-1.46%
Mezzanine loans (1)	14,004	100.40%	11,485	82.34%	(2,519 )	-18.06%
Loans held for sale (3)	19,528	100.14%	19,528	100.14%	–	–%
Preferred stock and warrants	31,213	100.00%	31,213	100.00%	–	–%
Total fixed rate	171,202	76.10%	173,436	77.10%	2,234	1.00%
Grand total	\$ 1,694,344	91.66%	\$ 1,661,726	89.90%	\$ (32,618 )	-1.76%
December 31, 2010						
Floating rate						
CMBS-private placement	\$ 31,127	100.00%	\$ 9,569	30.74%	\$ (21,558 )	-69.26%
Structured notes	7,984	34.09%	17,723	75.67%	9,739	41.58%
Other ABS	–	–%	22	0.26%	22	0.26%
B notes (1)	26,485	99.94%	26,071	98.38%	(414 )	-1.56%
Mezzanine loans (1)	83,699	100.00%	82,680	98.78%	(1,019 )	-1.22%
Whole loans (1)	441,372	99.92%	419,207	94.91%	(22,165 )	-5.01%
Bank loans (2)	856,436	96.99%	850,500	96.32%	(5,936 )	-0.67%
Loans held for sale (3)	13,593	55.92%	13,593	55.92%	–	–%
ABS held-to-maturity (4)	29,036	91.08%	25,941	81.37%	(3,095 )	-9.71%
Total floating rate	1,489,732	95.86%	1,445,306	93.01%	(44,426 )	-2.85%
Fixed rate						
CMBS – private placement	52,097	48.30%	54,369	50.41%	2,272	2.11%
B notes (1)	30,966	99.53%	30,482	97.97%	(484 )	-1.56%
Mezzanine loans (1)	38,545	100.23%	31,012	80.64%	(7,533 )	-19.59%
Loans held for sale (3)	15,000	75.00%	15,000	75.00%	–	–%
Lease receivables (5)	109,682	100.00%	109,612	99.94%	(70 )	-0.06%
Total fixed rate	246,290	80.20%	240,475	78.30%	(5,815 )	-1.90%
Grand total	\$ 1,736,022	93.28%	\$ 1,685,781	90.58%	\$ (50,241 )	-2.70%

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- (1) Net carrying amount includes an allowance for loan losses of \$25.9 million at March 31, 2011, allocated as follows: B notes (\$621,000), mezzanine loans (\$3.7 million) and whole loans (\$21.6 million). Net carrying amount includes an allowance for loan losses of \$31.6 million at December 31, 2010, allocated as follows: B notes (\$899,000), mezzanine loans (\$8.5 million) and whole loans (\$22.2 million).
- (2) The bank loan portfolio is carried at amortized cost less allowance for loan loss and was \$864.1 million at March 31, 2011. The amount disclosed represents net realizable value at March 31, 2011, which includes a \$1.8 million allowance for loan losses at March 31, 2011. The bank loan portfolio is carried at amortized cost less allowance for loan loss and was \$853.8 million at December 31, 2010. The amount disclosed represents net realizable value at December 31, 2010, which includes a \$2.6 million allowance for loan losses at December 31, 2010.
- (3) Loans held for sale are carried at the lower of cost or market. Amortized cost is equal to fair value.



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(4) ABS held-to-maturity are carried at amortized cost less other-than-temporary impairments.

Commercial Mortgage-Backed Securities-Private Placement. The determination of other-than-temporary impairment is a subjective process, and different judgments and assumptions could affect the timing of loss realization. We review our portfolios and make other-than-temporary impairment determinations at least quarterly. We consider the following factors when determining if there is an other-than-temporary impairment on a security:

the length of time the market value has been less than amortized cost;

the severity of the impairment;

the expected loss of the security as generated by third party software;

credit ratings from the rating agencies;

underlying credit fundamentals of the collateral backing the security; and

whether, based upon our intent, it is more likely than not that we will sell the security before the recovery of the amortized cost basis.

At March 31, 2011 and December 31, 2010, we held \$91.1 million and \$64.0 million, respectively, (net of net unrealized losses of \$14.4 million and \$19.3 million, respectively) of CMBS recorded at fair value. To determine fair value, we use two methods, either a dealer quote or an internal valuation model, depending upon the current level of market activity. As of March 31, 2011 and December 31, 2010, \$80.1 million and \$53.7 million, respectively, of investment securities available-for-sale were valued using dealer quotes and \$11.0 million and \$10.3 million, respectively, were valued using the weighted average of the three measures discussed below.

For securities with higher levels of market activity, we obtain a quote from a dealer, which typically will be the dealer who sold us the security. We have been advised that, in formulating their quotes, dealers may use recent trades in the particular security, if any, market activity in similar securities, if any, or internal valuation models. These quotes are non-binding. As a result of how the dealers develop their quotes, the market illiquidity and low levels of trading activity all of these securities had in the past been categorized in Level 3 in the fair value hierarchy. Due to the increased level of trading activity in 2010 and 2011, we moved some of these securities into Level 2 in the fair value hierarchy. We evaluate the reasonableness of the quotes we receive by applying our own valuation models. If there is a material difference between a quote we receive and the value indicated by our valuation models, we will evaluate the difference. As part of that evaluation, we will discuss the difference with the dealer, who may revise their quote based upon these discussions. Alternatively, we may revise our valuation models.

For investment securities available-for-sale with lower levels of market activity, we determine fair value based on taking a weighted average of the following three measures:

dealer quotes, as described above;

quotes on more actively-traded, higher-rated securities issued in a similar time period, adjusted for differences in rating and seniority; and

the value resulting from an internal valuation model using an income approach based upon an appropriate risk-adjusted yield, time value and projected losses using default assumptions based upon an historical analysis of underlying loan performance.

In the aggregate, we purchased our CMBS-private placement portfolio at a discount. At March 31, 2011 and December 31, 2010, the remaining discount to be accreted into income over the remaining lives of the securities was \$15.3 million and \$16.6 million, respectively. These securities are classified as available-for-sale and, as a result, are carried at their fair value.

There was no other-than temporary impairment recorded during the three months ended March 31, 2011 or 2010. While our securities classified as available-for-sale have declined in fair value on a net basis, we concluded that the decline continues to be temporary. We perform an on-going review of third-party reports and updated financial data on the underlying property financial information to analyze current and projected loan performance. Rating agency downgrades are considered with respect to our income approach when determining other-than-temporary impairment and, when inputs are stressed, the resulting projected cash flows reflect a full recovery of principal. We do not believe that any of our securities classified as available-for-sale were other-than-temporarily impaired as of March 31, 2011.

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The following table summarizes our CMBS-private placement (in thousands, except percentages):

	Fair Value at December 31, 2010	During Quarter Ended March 31, 2011			Fair Value at March 31, 2011
		Net Purchases	Upgrades/ Downgrades	MTM Change on Same Ratings	
<b>Moody's Ratings Category:</b>					
Aaa	\$ –	\$ 12,754	\$ –	\$ –	\$ 12,754
Aa1 through Aa3	4,493	–	–	(26 )	4,467
A1 through A3	18,570	–	–	916	19,486
Baa1 through Baa3	28,660	9,673	–	1,452	39,785
Ba1 through Ba3	1,480	–	–	1,640	3,120
B1 through B3	517	–	–	(158 )	359
Caa1 through Caa3	6,739	–	–	1,080	7,819
Ca through C	3,479	–	–	(203 )	3,276
Total	\$ 63,938	\$ 22,427	\$ –	\$ 4,701	\$ 91,066
<b>S&amp;P Ratings Category:</b>					
AAA	\$ –	\$ 12,754	\$ –	\$ –	\$ 12,754
A+ through A-	9,562	–	–	585	10,147
BBB+ through BBB-	36,385	9,673	(2,148 )	3,033	46,943
BB+ through BB-	7,690	–	–	380	8,070
B+ through B-	–	–	2,148	–	2,148
CCC+ through CCC-	10,220	–	–	701	10,921
D	81	–	–	2	83
Total	\$ 63,938	\$ 22,427	\$ –	\$ 4,701	\$ 91,066

Structured notes. The following table summarizes our structured notes, which are classified as investment securities, trading, which are carried at fair value (in thousands):

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
<b>March 31, 2011:</b>				
Structured notes	\$21,989	\$9,403	\$(122 )	\$31,270
Total	\$21,989	\$9,403	\$(122 )	\$31,270
<b>December 31, 2010:</b>				
Structured notes	\$7,984	\$9,739	\$–	\$17,723
Total	\$7,984	\$9,739	\$–	\$17,723

We purchased 18 securities and sold eight securities during the three months ended March 31, 2011, for a gain of \$2.3 million. We held 23 and 13 investment securities, trading as of March 31, 2011 and December 31, 2010, respectively.

Other Asset-Backed Securities. At March 31, 2011, we held two other ABS positions with a fair value of \$23,000. At December 31, 2010, we held two other ABS positions with a fair value of \$23,000. These securities are classified as available-for-sale and carried at fair value.



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Real Estate Loans. The following table is a summary of the loans in our commercial real estate loan portfolio at the dates indicated (in thousands):

Description	Number of Loans	Amortized Cost	Contracted Interest Rates	Maturity Dates (4)
<b>March 31, 2011:</b>				
Whole loans, floating rate (1)	27	\$ 460,081	LIBOR plus 1.50% to LIBOR plus 5.75%	May 2011 to May 2017
B notes, floating rate	2	24,242	LIBOR plus 2.50% to LIBOR plus 3.01%	July 2011 to October 2011
B notes, fixed rate	2	30,925	7.00% to 8.68%	July 2011 to April 2016
Mezzanine loans, floating rate	5	81,878	LIBOR plus 2.20% to LIBOR plus 3.00%	May 2011 to January 2013
Mezzanine loans, fixed rate (2)	4	33,532	8.65% to 11.00%	January 2016 to September 2016
<b>Total (3)</b>	<b>40</b>	<b>\$ 630,658</b>		
<b>December 31, 2010:</b>				
Whole loans, floating rate (1)	25	\$ 441,372	LIBOR plus 1.50% to LIBOR plus 5.75%	May 2011 to January 2018
B notes, floating rate	2	26,485	LIBOR plus 2.50% to LIBOR plus 3.01%	July 2011 to October 2011
B notes, fixed rate	2	30,966	7.00% to 8.68%	July 2011 to April 2016
Mezzanine loans, floating rate	6	93,266	LIBOR plus 2.15% to LIBOR plus 3.00%	May 2011 to January 2013
Mezzanine loans, fixed rate (2)	5	53,545	8.14% to 11.00%	January 2016 to September 2016
<b>Total (3)</b>	<b>40</b>	<b>\$ 645,634</b>		

(1) Whole loans had \$9.1 million and \$5.0 million in unfunded loan commitments as of March 31, 2011 and December 31, 2010, respectively. These commitments are funded as the loans require additional funding and the related borrowers have satisfied the requirements to obtain this additional funding.

(2)

Fixed rate mezzanine loan dates exclude a loan that matured in May 2010 and is in default and has been on non-accrual status as of December 31, 2010.

(3) The total does not include an allowance for loan losses of \$25.9 million and \$31.6 million recorded as of March 31, 2011 and December 31, 2010, respectively.

(4) Maturity dates do not include possible extension options that may be available to the borrowers.

Subsequent to March 31, 2011, we entered into and completed sale agreements for two commercial real estate loans. One loan is secured by a hotel portfolio in various locations that we sold at 85% of par, resulting in a loss of \$2.25 million of which \$235,000 had been previously allocated as part of our general reserve. The second loan is secured by an office tower in New York City that we sold at par, with transactions costs resulting in a loss of \$656,000. The third loan with a fair value of \$676,000 is secured by a pad for retail use in Arizona. We expect a sale to occur during 2011. We classified these loans as loans held for sale as of March 31, 2011.

Bank Loans. At March 31, 2011, we held a total of \$876.4 million of bank loans at fair value through Apidos CDO I, Apidos CDO III and Apidos Cinco CDO, including one loan held outside of the CDOs. All but the loan outside of the CDOs secure the debt issued by these entities. This is an increase of \$16.0 million over our holdings at December 31, 2010. The increase in total bank loans was principally due to improved market prices for bank loans. We own 100% of the equity issued by Apidos CDO I, Apidos CDO III and Apidos Cinco CDO which we have determined are VIEs of which we are the primary beneficiary. As a result, we consolidate Apidos CDO I, Apidos CDO III and Apidos Cinco CDO.

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The following table summarizes our bank loan investments as of March 31, 2011 and December 31, 2010 (in thousands, except percentages):

	March 31, 2011		December 31, 2010	
	Amortized cost	Fair Value	Amortized cost	Fair Value
<b>Moody's ratings category:</b>				
Baa1 through Baa3	\$ 26,604	\$ 26,805	\$ 27,262	\$ 27,505
Ba1 through Ba3	459,529	467,446	432,153	437,269
B1 through B3	331,332	330,772	351,147	347,664
Caa1 through Caa3	23,079	19,789	20,879	16,690
Ca	7,005	3,189	7,062	2,857
No rating provided	28,251	28,430	21,960	21,906
<b>Total</b>	<b>\$ 875,800</b>	<b>\$ 876,431</b>	<b>\$ 860,463</b>	<b>\$ 853,891</b>
<b>S&amp;P ratings category:</b>				
BBB+ through BBB-	\$ 62,282	\$ 62,643	\$ 54,560	\$ 55,004
BB+ through BB-	384,921	391,044	373,971	378,949
B+ through B-	358,469	360,019	360,581	358,068
CCC+ through CCC-	30,541	24,231	29,707	22,171
CC+ through CC-	1,633	1,369	1,633	1,279
C+ through C-	—	—	—	—
D	1,050	662	1,050	431
No rating provided	36,904	36,463	38,961	37,989
<b>Total</b>	<b>\$ 875,800</b>	<b>\$ 876,431</b>	<b>\$ 860,463</b>	<b>\$ 853,891</b>
<b>Weighted average rating factor</b>	<b>1,901</b>		<b>2,061</b>	

Asset-backed securities held-to-maturity. At March 31, 2011, we held a total of \$26.9 million of ABS held-to-maturity at fair value through Apidos CDO I, Apidos CDO III and Apidos Cinco CDO, all of which secure the debt issued by these entities. This is an increase of \$1.0 million over our holdings at December 31, 2010. The increase in total ABS held-to-maturity was principally due to the improved market prices.

The following table summarizes our ABS held-to-maturity, at cost as of March 31, 2011 and December 31, 2010 (in thousands, except percentages):

	March 31, 2011		December 31, 2010	
	Amortized cost	Fair Value	Amortized cost	Fair Value
<b>Moody's ratings category:</b>				
Aa1 through Aa3	\$ 2,699	\$ 2,924	\$ 2,766	\$ 3,025
A1 through A3	7,693	8,176	7,625	8,117
Baa1 through Baa3	2,875	2,875	1,950	1,950
Ba1 through Ba3	1,584	1,540	2,503	2,338
B1 through B3	6,534	5,471	4,998	3,881
Caa1 through Caa3	7,821	5,917	9,194	6,630
Ca	—	—	—	—
<b>Total</b>	<b>\$ 29,206</b>	<b>\$ 26,903</b>	<b>\$ 29,036</b>	<b>\$ 25,941</b>
<b>S&amp;P ratings category:</b>				

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AA+ through AA-	\$ 5,139	\$ 5,452	\$ 5,099	\$ 5,437
A+ through A-	5,253	5,648	5,292	5,705
BBB+ through BBB-	3,521	3,529	3,516	3,479
BB+ through BB-	393	309	3,062	2,765
B+ through B-	3,302	3,232	—	—
No rating provided	11,598	8,733	12,067	8,555
Total	\$ 29,206	\$ 26,903	\$ 29,036	\$ 25,941
Weighted average rating factor	3,107		3,105	



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The following table provides information as to the lien status of our bank loans. All, except \$850,000 of first lien loans, are held by the indicated CDOs, which we consolidate (in thousands):

	Amortized Cost (1)			Total
	Apidos I	Apidos III	Apidos Cinco	
<b>March 31, 2011:</b>				
Loans held for investment:				
First lien loans	\$292,994	\$242,795	\$298,658	\$834,447
Second lien loans	10,689	9,126	10,151	29,966
Subordinated second lien loans	163	122	–	285
Defaulted second lien loans	–	–	362	362
Total	303,846	252,043	309,171	865,060
First lien loans held for sale at fair value	4,442	2,472	2,976	9,890
Total	\$308,288	\$254,515	\$312,147	\$874,950
<b>December 31, 2010:</b>				
Loans held for investment:				
First lien loans	\$288,163	\$236,142	\$296,208	\$820,513
Second lien loans	12,902	10,011	11,513	34,426
Subordinated second lien loans	163	122	–	285
Defaulted second lien loans	–	–	362	362
Total	301,228	246,275	308,083	855,586
First lien loans held for sale at fair value	2,822	–	1,205	4,027
Total	\$304,050	\$246,275	\$309,288	\$859,613

(1) All loans are senior and secured unless otherwise noted.

Lease Receivables. Investments in lease receivables, net of unearned income, were as follows (in thousands):

	March 31, 2011	December 31, 2010
Leases, net of unearned income	\$–	\$75,908
Operating leases	–	17,900
Notes receivable	–	15,874
Subtotal	–	109,682
Allowance for lease losses	–	(70)
Total	\$–	\$109,612

On January 4, 2011, our wholly-owned subsidiary, Resource TRS, made a preferred investment in LCC, a newly-formed equipment financing subsidiary of LEAF Financial Corporation, or LEAF Financial, a subsidiary of Resource America. Resource TRS contributed capital of approximately \$26.2 million to LCC in the form of approximately \$5.2 million in cash, and \$21.0 million of equity interests in LEAF Funding 3, a wholly-owned subsidiary of Resource TRS. As part of the transaction, LEAF Financial contributed its assets relating to its equipment lease and note origination, servicing and finance business to LCC. Also, senior management personnel of LEAF Financial, or collectively, the Management Parties, contributed capital to LCC in the form of all of the shares of

common stock they owned in LEAF Financial in exchange for 10% of the shares of LCC common stock on a fully-diluted basis. The foregoing capital investments in LCC were made pursuant to a Transfer and Contribution Agreement among the registrant, LEAF Financial, LCC, Resource TRS and the Management Parties, or the TCA. This transaction resulted in the deconsolidation of our leasing operations.

Pursuant to the TCA, in return for Resource TRS's capital investments, LCC issued and delivered to Resource TRS 2,626.783 shares of LCC Series A preferred stock and warrants to purchase 4,800 shares of LCC common stock for an exercise price of \$0.01 per share, representing 48% of LCC's common stock on a fully-diluted basis, classified as securities available-for-sale on our consolidated balance sheet.

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As set forth in the TCA, on January 4, 2011, Resource TRS also delivered to LCC a Share Purchase Agreement, under which LCC is permitted to require Resource TRS to purchase up to an additional \$10.0 million of Preferred Stock on the terms set forth therein. The preferred stock carries a coupon of 10%, of which 2% is received in cash and 8% is paid in-kind.

Restricted cash. At March 31, 2011, we had restricted cash of \$159.6 million, which consisted of \$157.1 million of restricted cash in our five CDOs, and \$2.5 million held in a margin account related to our swap portfolio. At December 31, 2010, we had restricted cash of \$168.2 million, which consisted of \$160.5 million of restricted cash in our five CDOs, \$5.2 million of restricted cash in our leasing securitization and \$2.5 million held in a margin account, related to our swap portfolio. The decrease of \$8.6 million is primarily related to reinvestments in our CRE CDOs. The majority of this cash had not been reinvested as of December 31, 2010.

Interest Receivable. At March 31, 2011, we had interest receivable of \$5.6 million, which consisted of \$5.6 million of interest on our securities, loans and structured notes and \$9,000 of interest earned on escrow and sweep accounts. At December 31, 2010, we had interest receivable of \$6.3 million, which consisted of \$6.3 million of interest on our securities, loans and lease receivables and \$9,000 of interest earned on escrow and sweep accounts. The decrease of \$775,000 this decrease is primarily the result of a reduction of \$714,000 in interest receivable on structured notes due to the timing of when payments were due and received and a decrease of \$280,000 in interest receivable on our bank loan portfolio due to repayments and sales of positions during the three months ended March 31, 2011. The decrease was partially offset by an increase of \$169,000 related to intercompany loans and a \$40,000 increase in interest receivable on our commercial real estate loan portfolio due to the origination of two new loans.

Other Assets. The following table summarizes our other assets as of December 31, 2010 and 2009 (in thousands):

	March 31, 2011	December 31, 2010
Other receivables	\$312	\$1,374
Prepaid assets	1,104	590
Dividend receivable	661	-
Management fees receivable	956	-
Principal paydown	60	468
Total	\$3,093	\$2,432

Other assets increased \$661,000 to \$3.1 million as of March 31, 2011 from \$2.4 million as of December 31, 2010. This increase resulted primarily from the following:

an increase of \$514,000 in prepaid assets which is primarily related to the director and officer insurance policy and the timing of when it is paid;

an increase of \$661,000 in dividend receivables as a result of our January 2011 investment in LCC; and

an increase of \$956,000 in management fees receivables which are related to our investment in a subsidiary which entitles us to collect senior, subordinated and incentive fees related to five collateralized loan obligations. There were no such fees for the three months ended March 31, 2010.

The increase in other assets was partially offset by a decrease of \$1.1 million in other receivables principally due to receivables on our leasing portfolio which was sold on January 4, 2011. In addition principal paydowns decreased \$408,000 due to the timing of our receipt of payments on our leasing and bank loan portfolios.



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Hedging Instruments. Our hedges at March 31, 2011 and December 31, 2010 were fixed-for-floating interest rate swap agreements whereby we swapped the floating rate of interest on the liabilities we hedged for a fixed rate of interest. With the pending maturity of several agreements, we expect that the fair value of our hedges will modestly improve during the remainder of 2011. We intend to continue to seek such hedges for our floating rate debt in the future. Our hedges at March 31, 2011 were as follows (in thousands):

	Benchmark rate	Notional value	Strike rate	Effective date	Maturity date	Fair value
Interest rate swap	1 month LIBOR	\$ 12,965	4.63%	12/04/06	07/01/11	\$ (143 )
Interest rate swap	1 month LIBOR	1,071	0.31%	03/04/11	08/01/11	–
Interest rate swap	1 month LIBOR	3,239	0.30%	03/16/11	08/01/11	–
Interest rate swap	1 month LIBOR	12,150	5.44%	06/08/07	03/25/12	(611 )
Interest rate swap	1 month LIBOR	12,750	5.27%	07/25/07	08/06/12	(824 )
Interest rate swap	1 month LIBOR	1,022	0.64%	02/23/11	11/01/13	(1 )
Interest rate swap	1 month LIBOR	329	0.51%	03/18/11	11/01/13	–
Interest rate swap	1 month LIBOR	1,215	0.55%	03/28/11	11/01/13	–
Interest rate swap	1 month LIBOR	4,250	0.84%	03/31/11	01/18/14	(4 )
Interest rate swap	1 month LIBOR	4,143	1.93%	02/14/11	05/01/15	(26 )
Interest rate swap	1 month LIBOR	4,250	1.95%	04/01/11	03/18/16	(6 )
Interest rate swap	1 month LIBOR	34,176	4.13%	01/10/08	05/25/16	(2,031 )
Interest rate swap	1 month LIBOR	1,681	5.72%	07/09/07	10/01/16	(151 )
Interest rate swap	1 month LIBOR	1,880	5.68%	07/13/07	03/12/17	(314 )
Interest rate swap	1 month LIBOR	81,399	5.58%	06/08/07	04/25/17	(7,099 )
Interest rate swap	1 month LIBOR	1,726	5.65%	06/28/07	07/15/17	(149 )
Interest rate swap	1 month LIBOR	3,850	5.65%	07/19/07	07/15/17	(331 )
Interest rate swap	1 month LIBOR	4,023	5.41%	08/07/07	07/25/17	(319 )
<b>Total</b>		<b>\$ 186,119</b>	<b>4.75%</b>			<b>\$ (12,009 )</b>

In addition, we also had an interest rate cap agreement with a notional of \$14.8 million outstanding as of March 31, 2010 which reduced our exposure to variability in future cash flows attributable to LIBOR. The interest rate cap is a non-designated cash flow hedge and as a result the change in fair value is recorded through the consolidated statement

of operations. The interest rate cap had an effective date of January 8, 2009, has a maturity date of August 5, 2011 and has a cap rate of 2.00%. The interest rate cap had a fair value of \$60 as of December 31, 2010.

As of December 31, 2010, we had entered into hedges with a notional amount of \$166.8 million and maturities ranging from July 2011 to July 2017. At December 31, 2010, the fair value on our interest rate swap agreements was (\$13.3) million.

CMBS – Term Repurchase Facility. In February 2011, our wholly-owned subsidiaries, RCC Real Estate and RCC Commercial, entered into a master repurchase agreement with Wells Fargo Bank, National Association to be used as a warehouse facility to finance the purchase of commercial mortgage-backed securities. We guaranteed RCC Real Estate and RCC Commercial's performance of their obligations under the repurchase agreement. At March 31, 2011, RCC Real Estate had borrowed \$15.1 million, all of which we had guaranteed, less unamortized deferred debt issuance costs for a net of \$14.6 million. At March 31, 2011, borrowings under the repurchase agreement were secured by commercial mortgage-backed securities with an estimated fair value of \$17.5 million and had a weighted average interest rate of one-month LIBOR plus 1.25%, or 1.50% at March 31, 2011.

Collateralized Debt Obligations. As of March 31, 2011, we had executed and retained equity in five CDO transactions as follows:

In June 2007, we closed RREF CDO 2007-1, a \$500.0 million CDO transaction that provided financing for commercial real estate loans. The investments held by RREF CDO 2007-1 collateralized \$458.8 million of senior notes issued by the CDO vehicle, of which RCC Real Estate, Inc., or RCC Real Estate, a subsidiary of ours, purchased 100% of the class H senior notes, class K senior notes, class L senior notes and class M senior notes for \$68.0 million at closing, \$5.0 million of the Class J senior notes in February 2008, an additional \$2.5 million of the Class J senior notes in November 2009, and \$11.9 million of the Class E senior notes, \$11.9 million of the Class F senior notes and \$7.3 million of the Class G senior notes in December 2009, and \$250,000 of the Class J senior notes in January 2010. In addition, RREF 2007-1 CDO Investor, LLC, a subsidiary of RCC Real Estate, purchased a \$41.3 million equity interest representing 100% of the outstanding preference shares. At March 31, 2011, the notes issued to outside investors, net of repurchased notes, had a weighted average borrowing rate of 0.81%.

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In May 2007, we closed Apidos Cinco CDO, a \$350.0 million CDO transaction that provided financing for bank loans. The investments held by Apidos Cinco CDO collateralized \$322.0 million of senior notes issued by the CDO vehicle. RCC Commercial Inc., or RCC Commercial, a subsidiary of ours, purchased a \$28.0 million equity interest representing 100% of the outstanding preference shares. At March 31, 2011, the notes issued to outside investors had a weighted average borrowing rate of 0.82%.

In August 2006, we closed RREF CDO 2006-1, a \$345.0 million CDO transaction that provided financing for commercial real estate loans. The investments held by RREF CDO 2006-1 collateralized \$308.7 million of senior notes issued by the CDO vehicle. RCC Real Estate purchased 100% of the class J senior notes and class K senior notes for \$43.1 million at closing and \$7.5 million of the Class F senior notes in June 2009, \$3.5 million of the Class E senior note and \$4.0 million of the Class F senior notes in September 2009 and \$20.0 million of the Class A-1 senior notes in February 2010. In addition, RREF 2006-1 CDO Investor, LLC, a subsidiary of RCC Real Estate, purchased a \$36.3 million equity interest representing 100% of the outstanding preference shares. At March 31, 2011, the notes issued to outside investors, net of repurchased notes, had a weighted average borrowing rate of 1.32%.

In May 2006, we closed Apidos CDO III, a \$285.5 million CDO transaction that provided financing for bank loans. The investments held by Apidos CDO III collateralized \$262.5 million of senior notes issued by the CDO vehicle. RCC Commercial purchased a \$23.0 million equity interest representing 100% of the outstanding preference shares. At March 31, 2011, the notes issued to outside investors had a weighted average borrowing rate of 0.76%.

In August 2005, we closed Apidos CDO I, a \$350.0 million CDO transaction that provided financing for bank loans. The investments held by Apidos CDO I collateralize \$321.5 million of senior notes issued by the CDO vehicle. RCC Commercial purchased a \$28.5 million equity interest representing 100% of the outstanding preference shares. At March 31, 2011, the notes issued to outside investors had a weighted average borrowing rate of 0.88%.

Trust Preferred Securities. In May and September 2006, we formed Resource Capital Trust I, or RCT I, and RCC Trust II, or RCT II, respectively, for the sole purpose of issuing and selling trust preferred securities. Resource Capital Trust I and RCC Trust II are not consolidated into our consolidated financial statements because we are not deemed to be the primary beneficiary of either trust. We own 100% of the common shares of each trust, each of which issued \$25.0 million of preferred shares to unaffiliated investors. Our rights as the holder of the common shares of each trust are subordinate to the rights of the holders of preferred shares only in the event of a default; otherwise, our economic and voting rights are pari passu with the preferred shareholders. We record each of our investments in the trusts' common shares of \$774,000 as an investment in unconsolidated trusts and record dividend income upon declaration by each trust. The junior subordinated debentures' debt issuance costs are deferred in other assets in the consolidated balance sheets. We record interest expense on the junior subordinated debentures and amortization of debt issuance costs in our consolidated statements of income.

In October 2009, we amended our unsecured junior subordinated debentures held by RCT I and RCT II with a total value outstanding of \$51.5 million. The amendment provides for an interest rate increase of 2% (from LIBOR plus 3.95% to LIBOR plus 5.95%) on both issuances for a period of two years and a one-time restructuring fee of \$250,000 in exchange for the waiver of financial covenants under our guarantee. The covenant waiver expires on January 1, 2012. The debt issuance costs associated with the junior subordinated debentures for RCT I and RCT II at March 31, 2011 were \$39,000 and \$38,000, respectively. The interest rate adjustment took effect as of October 1, 2009 and expires on September 30, 2011. The rates for RCT I and RCT II at March 31, 2011, were 6.26% and 6.25%, respectively. The rates for RCT I and RCT II at December 31, 2010, were 6.25% and 6.24%, respectively. The additional cost is approximately \$280,000 per quarter.





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## Financing Receivables

The following tables show the allowance for loan and lease receivable losses and recorded investments in loans and lease receivables at the dates indicated (in thousands):

	Commercial Real Estate Loans	Bank Loans	Loans Receivable- Related Party	Total
March 31, 2011:				
Allowance for losses at January 1, 2011	\$ 31,617	\$ 2,616	\$ –	\$ 34,233
Provision for loan loss	3,121	(515 )	–	2,606
Loans charged-off	(8,900 )	(270 )	–	(9,170 )
Recoveries	–	–	–	–
Allowance for losses at March 31, 2011	\$ 25,838	\$ 1,831	\$ –	\$ 27,669
Ending balance:				
Individually evaluated for impairment	\$ 15,300	\$ 112	\$ –	\$ 15,412
Collectively evaluated for impairment	\$ 10,538	\$ 1,719	\$ –	\$ 12,257
Loans acquired with deteriorated credit quality	\$ –	\$ –	\$ –	\$ –
Loans:				
Ending balance:				
Individually evaluated for impairment	\$ 36,000	\$ 362	\$ –	\$ 36,362
Collectively evaluated for impairment	\$ 594,658	\$ 875,438	\$ 9,689	\$ 1,479,785
Loans acquired with deteriorated credit quality	\$ –	\$ –	\$ –	\$ –

	Commercial Real Estate Loans	Bank Loans	Lease Receivables	Loans Receivable-Related Party	Total
December 31, 2010:					
Allowance for losses at January 1, 2010	\$ 29,297	\$ 17,825	\$ 1,140	\$ –	\$ 48,262
Provision for loan loss	44,357	(1,348 )	312	–	43,321
Loans charged-off	(42,037 )	(13,861 )	(1,432 )	–	(57,330 )
Recoveries	–	–	50	–	50
Allowance for losses at December 31, 2010	\$ 31,617	\$ 2,616	\$ 70	\$ –	\$ 34,303
Ending balance:					
Individually evaluated for impairment	\$ 20,844	\$ 112	\$ –	\$ –	\$ 20,956
Collectively evaluated for impairment	\$ 10,773	\$ 2,504	\$ 70	\$ –	\$ 13,347
Loans acquired with deteriorated credit quality	\$ –	\$ –	\$ –	\$ –	\$ –

## Loans:

## Ending balance:

Individually evaluated for impairment	\$42,219	\$362	\$ 10,024	\$ -	\$52,605
Collectively evaluated for impairment	\$603,415	\$860,101	\$ 99,658	\$ 9,927	\$1,573,101
Loans acquired with deteriorated credit quality	\$-	\$-	\$ -	\$ -	\$-

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## Credit quality indicators

## Bank Loans

We use a risk grading matrix to assign grades to bank loans. Loans are graded at inception and updates to assigned grades are made continually as new information is received. Loans are graded on a scale of 1-5 with 1 representing our highest rating and 5 representing our lowest rating. We also designate loans that are sold after the period then ended as such at their fair market value, net of any allowances and costs associated with the loan sales. We consider such things as performance of the underlying company, liquidity, collectability of interest, enterprise valuation, default probability, ratings from rating agencies, and industry dynamics.

Credit risk profiles of bank loans were as follows (in thousands):

	Rating 1	Rating 2	Rating 3	Rating 4	Rating 5	Held for Sale	Total
As of March 31, 2011:							
Bank loans	\$787,108	\$31,150	\$41,330	\$5,960	\$362	\$9,890	\$875,800
As of December 31, 2010:							
Bank loans	\$759,162	\$43,858	\$45,115	\$7,940	\$362	\$4,027	\$860,464

All of our bank loans are performing with the exception of one loan with a par amount of \$362,000 which has been in default since September 2010.

## Commercial Real Estate Loans

We use a risk grading matrix to assign grades to commercial real estate loans. Loans are graded at inception and updates to assigned grades are made continually as new information is received. Loans are graded on a scale of 1-4 with 1 representing our highest rating and 4 representing our lowest rating. We also designate loans that are sold after the period then ended as such at their fair market value, net of any allowances and costs associated with the loan sales. In addition to the underlying performance of the loan collateral, we consider such things as the strength of underlying sponsorship, payment history, collectability of interest, structural credit enhancements, market trends and loan terms.

Credit risk profiles of commercial real estate loans were as follows (in thousands):

	Rating 1	Rating 2	Rating 3	Rating 4	Held for Sale	Total
As of March 31, 2011:						
Whole loans	\$169,503	\$45,559	\$208,343	\$36,000	\$676	\$460,081
B notes	16,508	11,492	14,417	–	12,750	55,167
Mezzanine loans	7,525	33,805	54,552	–	19,528	115,410
	\$193,536	\$90,856	\$277,312	\$36,000	\$32,954	\$630,658
As of December 31, 2010:						
Whole loans	\$123,350	\$16,143	\$264,660	\$37,219	\$–	\$441,372
B notes	16,538	–	40,913	–	–	57,451
Mezzanine loans	32,635	–	84,610	5,000	24,566	146,811

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\$172,523      \$16,143      \$390,183      \$42,219      \$24,566      \$645,634

As of March 31, 2011, all of our commercial real estate loans are performing. As of December 31, 2010 all of our commercial real estate loans are performing with the exception of one loan with a par amount of \$5.0 million which has been in default since May 2010. This position was charged off as of March 31, 2011.

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## Loan and Lease Receivable Portfolios Aging Analysis

The following tables show the loan and lease receivable portfolio aging analysis at the dates indicated at cost basis (in thousands):

	30-59 Days	60-89 Days	Greater than 90 Days	Total Past Due	Current	Total Loans Receivable	Total Loans > 90 Days and Accruing
<b>March 31, 2011:</b>							
Whole loans	\$ -	\$ -	\$ -	\$ -	\$ 460,081	\$ 460,081	\$ -
B notes	-	-	-	-	55,167	55,167	-
Mezzanine loans	-	-	-	-	115,410	115,410	-
Bank loans	-	-	362	362	875,438	875,800	-
Loans receivable- related party	-	-	-	-	9,689	9,689	-
<b>Total loans</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 362</b>	<b>\$ 362</b>	<b>\$ 1,515,785</b>	<b>\$ 1,516,147</b>	<b>\$ -</b>
<b>December 31, 2010:</b>							
Whole loans	\$ -	\$ -	\$ -	\$ -	\$ 441,372	\$ 441,372	\$ -
B notes	-	-	-	-	57,451	57,451	-
Mezzanine loans	-	-	5,000	5,000	141,811	146,811	-
Bank loans	-	-	-	-	860,463	860,463	-
Lease receivables	630	237	829	1,696	107,986	109,682	-
Loans receivable- related party	-	-	-	-	9,927	9,927	-
<b>Total loans</b>	<b>\$ 630</b>	<b>\$ 237</b>	<b>\$ 5,829</b>	<b>\$ 6,696</b>	<b>\$ 1,619,010</b>	<b>\$ 1,625,706</b>	<b>\$ -</b>

## Impaired Loans and Lease Receivables

The following tables show impaired loans and lease receivables (in thousands):

	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Average Investment in Impaired Loans	Interest Income Recognized
<b>March 31, 2011:</b>					
Loans and lease receivables without a specific valuation allowance:					
Whole loans	\$112,433	(1)	\$112,433	\$-	\$111,959
					\$513

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B notes	-	-	-	-	-
Mezzanine loans	-	-	-	-	-
Bank loans	-	-	-	-	-
Loans and lease receivables with a specific valuation allowance:					
Whole loans	36,000	36,000	(15,300 )	35,880	227
B notes	-	-	-	-	-
Mezzanine loans	-	-	-	5,000	-
Bank loans	362	362	(112 )	362	-
Total:					
Whole loans	\$148,433	\$148,433	\$(15,300 )	\$147,839	\$740
B notes	-	-	-	-	-
Mezzanine loans	-	-	-	5,000	-
Bank loans	362	362	(112 )	362	-
	\$148,795	\$148,795	\$(15,412 )	\$153,201	\$740

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	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Average Investment in Impaired Loans	Interest Income Recognized
December 31, 2010:					
Loans and lease receivables without a specific valuation allowance:					
Whole loans	\$ 111,401 (1)	\$ 111,401	\$ –	\$ 58,058	\$ 1,133
B notes	–	–	–	–	–
Mezzanine loans	–	–	–	–	–
Bank loans	–	–	–	–	–
Lease receivables	–	–	–	–	–
Loans and lease receivables with a specific valuation allowance:					
Whole loans	37,219	37,219	(15,844 )	36,740	993
B notes	–	–	–	–	–
Mezzanine loans	5,000	5,000	(5,000 )	5,000	–
Bank loans	362	362	(112 )	8,971	–
Lease receivables	10,024	10,024	(4,107 )	4,791	–
<b>Total:</b>					
Whole loans	\$ 148,620	\$ 148,620	\$ (15,844 )	\$ 94,798	\$ 2,126
B notes	–	–	–	–	–
Mezzanine loans	5,000	5,000	(5,000 )	5,000	–
Bank loans	362	362	(112 )	8,971	–
Lease receivables	10,024	10,024	(4,107 )	4,791	–
	\$ 164,006	\$ 164,006	\$ (25,063 )	\$ 113,560	\$ 2,126

(1) Specific allowances were not taken on whole loans of \$112.4 million and \$111.4 million of par value as of March 31, 2011 and December 31, 2010, respectively that were evaluated for and deemed to be troubled debt restructurings, or TDRs. These TDRs do not have an associated specific loan loss allowance because the principal and interest amount is considered recoverable based on expected collateral performance and / or guarantees made by the borrowers.

### Stockholders' Equity

Stockholders' equity at March 31, 2011 was \$427.2 million and included \$14.4 million of net unrealized losses on our available-for-sale portfolio, and \$13.3 million of unrealized losses on cash flow hedges, shown as a component of accumulated other comprehensive loss. Stockholders' equity at December 31, 2010 was \$348.3 million and included \$19.3 million of unrealized losses on our available-for-sale portfolio and \$13.3 million of unrealized losses on cash flow hedges, shown as a component of accumulated other comprehensive loss. The increase in stockholder's equity during the three months ended March 31, 2011 was principally due to the proceeds received related to our stock offering in March 2011 and our DRIP during the quarter.

Fluctuations in market values of assets in our available-for-sale portfolio that have not been other-than-temporarily impaired, do not impact our income determined in accordance with GAAP, or our taxable income, but rather are reflected on our consolidated balance sheets by changing the carrying value of the asset and stockholders' equity under "Accumulated Other Comprehensive Loss."

The following table reconciles GAAP net income to adjusted net income, which is a non-GAAP financial measure. (in thousands):

	Three Months Ended March 31,	
	2011	2010
Net income – GAAP	\$13,142	\$1,406
Adjustments:		
Provision for loan and lease losses (2)	2,606	15,371
Gains on the extinguishment of debt	–	(6,628 )
Adjusted net income, excluding non-cash items (1)	\$15,748	\$10,149
Adjusted net income per share – diluted, excluding non-cash items	\$0.26	\$0.27



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(1) During 2010, we evaluated our performance based on several performance measures, including adjusted net income, in addition to net income and estimated REIT taxable income. Adjusted net income represents net income available to common shares, computed in accordance with GAAP, before provision for loan and lease losses, gain on the extinguishment of debt and non-operating capital items. These items are recorded in accordance with GAAP and are typically non-cash or non-operating items that do not impact our operating performance or ability to pay a dividend.

Management views adjusted net income as a useful and appropriate supplement to GAAP net income because it helps management evaluate our performance without the effects of certain GAAP adjustments that may not have a direct financial impact on our current operating performance and dividend paying ability. Management uses adjusted net income to evaluate the performance of our investment portfolios, ability to manage its expenses and dividend paying ability before the impact of non-cash adjustments and non-operating capital gain or loss recorded in accordance with GAAP. We believe this is a useful performance measure for investors to evaluate these aspects of our business as well. The most significant adjustments we exclude in determining adjusted earnings as of March 31, 2011 and 2010 are the provision for loan and lease losses, loss from asset impairments and gain on the extinguishment of debt. Management excludes all such items from our calculation of adjusted net income because these items are not charges or losses which would impact our current operating performance. However, by excluding these significant items, adjusted net income reduces an investor's understanding of our operating performance by excluding management's expectation of possible future gains or losses from our investment portfolio.

Adjusted net income, as a non-GAAP financial measurement, does not purport to be an alternative to GAAP net income, or a measure of operating performance or cash flows from operating activities determined in accordance with GAAP as a measure of liquidity. Instead, adjusted net income should be reviewed in connection with net income and cash flows from operating, investing and financing activities in our consolidated financial statements to help analyze management's expectation of potential future losses from our investment portfolio and other non-cash or capital matters that impact our financial results. Adjusted net income and other supplemental performance measures are defined in various ways throughout the REIT industry. Investors should consider these differences when comparing our adjusted net income to these other REITs.

(2) Non-cash charges for loan and lease losses.

#### Estimated REIT Taxable Income

We calculate estimated REIT taxable income, which is a non-GAAP financial measure, according to the requirements of the Internal Revenue Code. The following table reconciles net income to estimated REIT taxable income for the periods presented (in thousands):

	Three Months Ended March 31,	
	2011	2010
Net income – GAAP	\$ 13,142	\$ 1,406
Taxable REIT subsidiary's (income) loss	(2,004 )	(125 )
Adjusted net income	11,138	1,281
Adjustments:		
Share-based compensation to related parties	(93 )	(316 )
Provision for loan and lease losses unrealized	3,122	15,500
Equity in income of real estate joint venture	(4,473 )	–

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Net book to tax adjustment for the inclusion of our taxable foreign REIT subsidiaries	(1,098 )	(6,378 )
Subpart F income limitation (2)	–	322
Other net book to tax adjustments	11	(1,083 )
Estimated REIT taxable income	\$8,607	\$9,326
 Amounts per share – diluted	 \$0.14	 \$0.24

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(1) We believe that a presentation of estimated REIT taxable income provides useful information to investors regarding our financial condition and results of operations as this measurement is used to determine the amount of dividends that we are required to declare to our stockholders in order to maintain our status as a REIT for federal income tax purposes. Since we, as a REIT, expect to make distributions based on estimated REIT taxable income, we expect that our distributions may at times be more or less than our reported GAAP net income. Total estimated REIT taxable income is the aggregate amount of estimated REIT taxable income generated by us and by our domestic and foreign taxable REIT subsidiaries. Estimated REIT taxable income excludes the undistributed taxable income (if any) of our domestic taxable REIT subsidiary, which is not included in REIT taxable income until distributed to us. There is no requirement that our domestic taxable REIT subsidiary distribute its income to us. Estimated REIT taxable income, however, includes the taxable income of our foreign taxable REIT subsidiaries because we generally will be required to recognize and report their taxable income on a current basis. Because not all companies use identical calculations, this presentation of estimated REIT taxable income may not be comparable to other similarly-titled measures of other companies.

(2) U.S. shareholders of controlled foreign corporations are required to include their share of such corporations' income on a current basis; however, losses sustained by such corporations do not offset income of their U.S. shareholders on a current basis.

We believe that a presentation of estimated REIT taxable income provides useful information to investors regarding our financial condition and results of operations as we use this measurement to determine the amount of dividends that we are required to declare to our stockholders in order to maintain our status as a REIT for federal income tax purposes. Since we, as a REIT, expect to make distributions based on estimated taxable earnings, we expect that our distributions may at times be more or less than our reported GAAP earnings. Total taxable income is the aggregate amount of taxable income generated by us and by our domestic and foreign taxable REIT subsidiaries. Estimated REIT taxable income excludes the undistributed taxable income of our domestic TRS, if any such income exists, which is not included in REIT taxable income until distributed to us. There is no requirement that our domestic TRS distribute its earnings to us. Estimated REIT taxable income, however, includes the taxable income of our foreign TRSs because we are generally required to recognize and report their taxable income on a current basis. Because not all companies use identical calculations, this presentation of estimated REIT taxable income may not be comparable to other similarly-titled measures of other companies.

In order to maintain our qualification as a REIT and to avoid corporate-level income tax on the income we distribute to our stockholders, we intend to make regular quarterly distributions of all or substantially all of our estimated net REIT taxable income to holders of our common stock. This requirement can impact our liquidity and capital resources.

#### Liquidity and Capital Resources

As of March 31, 2011, our principal sources of current liquidity were \$46.6 million of net proceeds from our March 2011 offering and \$30.1 million of proceeds from sales of common stock through our DRIP and funds available in existing CDO financings of \$157.1 million at March 31, 2011. As of December 31, 2010, our principal sources of current liquidity were \$42.8 million of net proceeds from our May 2010 offering and \$76.8 million of proceeds from sales of common stock through our DRIP, funds available in existing CDO financings of \$160.5 million and \$84.9 million of availability under our repurchase agreement with Wells Fargo Bank, National Association to finance the purchase of CMBS.

Our on-going liquidity needs consist principally of funds to make investments, make debt repurchases, make distributions to our stockholders and pay our operating expenses, including our management fees. Our ability to meet our on-going liquidity needs will be subject to our ability to generate cash from operations and, with respect to our

investments, our ability to maintain and/or obtain additional debt financing and equity capital together with the funds referred to above. Historically, we have financed a substantial portion of our portfolio investments through CDOs that essentially match the maturity and repricing dates of these financing vehicles with the maturities and repricing dates of our investments. We derive substantial operating cash from our equity investments in our CDOs which, if the CDOs fail to meet certain tests, will cease. Through March 31, 2011, we have not experienced difficulty in maintaining our existing CDO financing and have passed all of the critical tests required by these financings. However, we cannot assure you that we will continue to meet all such critical tests in the future. If we are unable to renew, replace or expand our sources of existing financing on substantially similar terms, we may be unable to implement our investment strategies successfully and may be required to liquidate portfolio investments. If required, a sale of portfolio investments could be at prices lower than the carrying value of such assets, which would result in losses and reduced income.

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The following table sets forth collateralized debt obligations – distributions and coverage test summary for the periods presented (in thousands):

Name	CDO Type	Cash Distributions		Annualized Interest Coverage Cushion	Overcollateralization Cushion	
		Year Ended December 31, 2010 (1) (actual)	Three Months Ended March 31, 2011 (1) (actual)	As of March 31, 2011 (2) (3)	As of March 31, 2011 (4)	As of Initial Measurement Date
Apidos CDO I	CLO	\$ 7,695	\$ 2,057	\$ 9,639	\$ 14,181	\$ 17,136
Apidos CDO III	CLO	\$ 6,552	\$ 1,961	\$ 3,885	\$ 8,951	\$ 11,269
Apidos Cinco CDO	CLO	\$ 7,792	\$ 2,304	\$ 5,189	\$ 21,906	\$ 17,774
RREF 2006-1	CRE CDO	\$ 8,929	\$ 1,773	\$ 6,407	\$ 10,512	\$ 24,941
RREF 2007-1	CRE CDO	\$ 15,068	\$ 3,317	\$ 8,355	\$ 10,857	\$ 26,032

(1) Distributions on retained equity interests in CDOs (comprised of note investment and preference share ownership).

(2) Interest coverage includes annualized amounts based on the most recent trustee statements.

(3) Interest coverage cushion represents the amount by which annualized interest income expected exceeds the annualized amount payable on all classes of CDO notes senior to our preference shares.

(4) Overcollateralization cushion represents the amount by which the collateral held by the CDO issuer exceeds the maximum amount required.

At April 30, 2011, after paying the first quarter dividend, RCC's liquidity of \$207.8 million consists of two primary sources:

unrestricted cash and cash equivalents of \$38.3 million and restricted cash of \$2.0 million in margin call accounts;  
and

capital available for reinvestment in its five CDO entities of \$167.5 million, of which \$0.7 million is designated to finance future funding commitments on CRE loans.

Our leverage ratio may vary as a result of the various funding strategies we use. As of March 31, 2011 and December 31, 2010, our leverage ratio was 3.6 times and 4.4 times, respectively. The decrease in leverage ratio was primarily due to the March 2011 offering proceeds and DRIP proceeds received, during the three months ended March 31, 2011.

#### Distributions

In order to maintain our qualification as a REIT and to avoid corporate-level income tax on the income we distribute to our stockholders, we intend to make regular quarterly distributions of all or substantially all of our net taxable

income to holders of our common stock. This requirement can impact our liquidity and capital resources. On March 18, 2011, we declared a quarterly distribution of \$0.25 per share of common stock, \$17.6 million in the aggregate, which was paid on April 28, 2011 to stockholders of record on March 31, 2011.

Our 2011 dividends will be determined by our board of directors who will also consider the composition of any common dividends declared, including the option of paying a portion in cash and the balance in additional common shares. Generally, dividends payable in stock are not treated as dividends for purposes of the deduction for dividends, or as taxable dividends to the recipient. The Internal Revenue Service, in Revenue Procedure 2010-12, has given guidance with respect to certain stock distributions by publicly traded REITs. That Revenue Procedure applies to distributions made on or after January 1, 2008 and declared with respect to a taxable year ending on or before December 31, 2011. It provides that publicly-traded REITs can distribute stock (common shares in our case) to satisfy their REIT distribution requirements if stated conditions are met. These conditions include that at least 10% of the aggregate declared distributions be paid in cash and the shareholders be permitted to elect whether to receive cash or stock, subject to the limit set by the REIT on the cash to be distributed in the aggregate to all shareholders. We have not used this Revenue Procedure with respect to any distributions to date, but we are permitted to do so for distributions with respect to 2011.

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## Contractual Obligations and Commitments

	Contractual Commitments (dollars in thousands)				
	Payments due by period				
	Total	Less than 1 year	1 – 3 years	3 – 5 years	More than 5 years
CDOs (1)	\$1,398,653	\$–	\$–	\$–	\$1,398,653
Repurchase Agreements (2)	15,115	15,115	–	–	–
Unsecured junior subordinated debentures (3)	51,548	–	–	–	51,548
Base management fees (4)	7,016	7,016	–	–	–
<b>Total</b>	<b>\$1,472,332</b>	<b>\$22,131</b>	<b>\$–</b>	<b>\$–</b>	<b>\$1,450,201</b>

(1) Contractual commitments do not include \$21.4 million, \$29.6 million, \$24.2 million, \$30.9 million and \$55.4 million of interest expense payable through the non-call dates of July 2010, May 2011, June 2011, August 2011 and June 2012, respectively, on Apidos CDO I, Apidos Cinco CDO, Apidos CDO III, RREF 2006-1 and RREF 2007-1. The non-call date represents the earliest period under which the CDO assets can be sold, resulting in repayment of the CDO notes.

(2) Contractual commitments includes \$5,000 of interest expense payable through the maturity date of April 18, 2011 on our repurchase agreements.

(3) Contractual commitments do not include \$56.1 million and \$57.2 million of interest expense payable through the maturity dates of June 2036 and October 2036, respectively, on our trust preferred securities.

(4) Calculated only for the next 12 months based on our current equity, as defined in our management agreement. Our management agreement also provides for an incentive fee arrangement that is based on operating performance. Because the incentive fee is not a fixed and determinable amount, it is not included in this table.

At March 31, 2011, we had 18 interest rate swap contracts with a notional value of \$186.1 million. These contracts are fixed-for-floating interest rate swap agreements under which we contracted to pay a fixed rate of interest for the term of the hedge and will receive a floating rate of interest. As of March 31, 2011, the average fixed pay rate of our interest rate hedges was 4.75% and our receive rate was one-month LIBOR, or 0.25%. In addition, we also had an interest rate cap agreement with a notional amount of \$14.8 million outstanding which reduced our exposure to variability in future cash flows attributable to LIBOR. The interest rate cap is a non-designated cash flow hedge and, as a result, the change in fair value is recorded through our consolidated statements of income.

## Off-Balance Sheet Arrangements

As of March 31, 2011, we did not maintain any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance, special purpose or variable interest entities, established for the purpose of facilitating off-balance sheet arrangements or contractually narrow or limited purposes. Further, as of March 31, 2010, we had not guaranteed any obligations of unconsolidated entities or entered into any commitment or letter of intent to provide additional funding to any such entities.

We have certain unfunded commitments related to our commercial real estate loan portfolio that we may be required to fund in the future. Our unfunded commitments generally fall into two categories: (1) pre-approved capital

improvement projects; and (2) new or additional construction costs subject, in each case, to the borrower meeting specified criteria. Upon completion of the improvements or construction, we would receive additional loan interest income on the advanced amount. As of March 31, 2011, we had six loans with unfunded commitments totaling \$9.1 million, of which \$940,000 will be funded by restricted cash in RREF CDO 2007-1.



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### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As of March 31, 2011 and December 31, 2010, the primary component of our market risk was interest rate risk, as described below. While we do not seek to avoid risk completely, we do seek to assume risk that can be quantified from historical experience, to actively manage that risk, to earn sufficient compensation to justify assuming that risk and to maintain capital levels consistent with the risk we undertake or to which we are exposed.

We primarily assess our interest rate risk by estimating the duration of our assets and the duration of our liabilities. Duration essentially measures the market price volatility of financial instruments as interest rates change. We generally calculate duration using various financial models and empirical data. Different models and methodologies can produce different duration numbers for the same securities.

The following sensitivity analysis tables show, at March 31, 2011 and December 31, 2010, the estimated impact on the fair value of our interest rate-sensitive investments and liabilities of changes in interest rates, assuming rates instantaneously fall 100 basis points and rise 100 basis points (dollars in thousands):

	March 31, 2011		
	Interest rates fall 100 basis points	Unchanged	Interest rates rise 100 basis points
<b>CMBS – private placement (1)</b>			
Fair value	\$60,783	\$58,090	\$55,524
Change in fair value	\$2,693	\$–	\$(21,566 )
Change as a percent of fair value	4.64%	–%	4.42%
<b>Hedging instruments</b>			
Fair value	\$(26,399 )	\$(12,009 )	\$(6,162 )
Change in fair value	\$(14,390 )	\$–	\$7,130
Change as a percent of fair value	119.83%	–%	53.64%
	December 31, 2010		
	Interest rates fall 100 basis points	Unchanged	Interest rates rise 100 basis points
<b>CMBS – private placement (1):</b>			
Fair value	\$56,491	\$54,125	\$51,939
Change in fair value	\$2,336	\$–	\$(2,216 )
Change as a percent of fair value	4.31%	–%	4.09%
<b>Hedging instruments:</b>			
Fair value	\$(20,622 )	\$(13,292 )	\$(6,162 )
Change in fair value	\$(7,330 )	\$–	\$7,130
Change as a percent of fair value	55.15%	–%	53.64%

(1) Includes the fair value of available-for-sale investments that are sensitive to interest rate change.

For purposes of the table, we have excluded our investments with variable interest rates that are indexed to LIBOR. Because the variable rates on these instruments are short-term in nature, we are not subject to material exposure to movements in fair value as a result of changes in interest rates.

#### Effect on Fair Value

A component of interest rate risk is the effect changes in interest rates will have on the market value of our assets. We face the risk that the market value of our assets will increase or decrease at different rates than that of our liabilities, including our hedging instruments.

It is important to note that the impact of changing interest rates on fair value can change significantly when interest rates change beyond 100 basis points from current levels. Therefore, the volatility in the fair value of our assets could increase significantly when interest rates change beyond 100 basis points from current levels. In addition, other factors impact the fair value of our interest rate-sensitive investments and hedging instruments, such as the shape of the yield curve, market expectations as to future interest rate changes and other market conditions. Accordingly, in the event of changes in actual interest rates, the change in the fair value of our assets would likely differ from that shown above and such difference might be material and adverse to our stockholders.

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## Risk Management

To the extent consistent with maintaining our status as a REIT, we seek to manage our interest rate risk exposure to protect our portfolio of fixed-rate commercial real estate mortgages and CMBS and related debt against the effects of major interest rate changes. We generally seek to manage our interest rate risk by:

monitoring and adjusting, if necessary, the reset index and interest rate related to our mortgage-backed securities and our borrowings;

attempting to structure our borrowing agreements for our CMBS to have a range of different maturities, terms, amortizations and interest rate adjustment periods; and

using derivatives, financial futures, swaps, options, caps, floors and forward sales, to adjust the interest rate sensitivity of our fixed-rate commercial real estate mortgages and CMBS and our borrowing.

## ITEM 4. CONTROLS AND PROCEDURES

### Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Securities Exchange Act of 1934 reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, our management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Under the supervision of our Chief Executive Officer and Chief Financial Officer, we have carried out an evaluation of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective at the reasonable assurance level.

### Changes in Internal Control of Financial Reporting

There were no significant changes in our internal control over financial reporting during the quarter ended March 31, 2011, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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## PART II. OTHER INFORMATION

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) In accordance with the provisions of the management agreement, on January 31, 2011, we issued 4,482 shares of common stock to the Manager. These shares represented 25% of the Manager's quarterly incentive compensation fee that accrued for the three months ended December 31, 2010. The issuance of these shares was exempt from the registration requirements of the Securities Act pursuant to Section 4(2) thereof.

## ITEM 5. EXHIBITS

Exhibit No.	Description
3.1	Restated Certificate of Incorporation of Resource Capital Corp. (1)
3.2	Amended and Restated Bylaws of Resource Capital Corp. (1)
4.1	Form of Certificate for Common Stock for Resource Capital Corp. (1)
4.2(a)	Junior Subordinated Indenture between Resource Capital Corp. and Wells Fargo Bank, N.A., dated May 25, 2006. (2)
4.2(b)	Amendment to Junior Subordinated Indenture and Junior Subordinated Note due 2036 between Resource Capital Corp. and Wells Fargo Bank, N.A., dated October 26, 2009 and effective September 30, 2009. (6)
4.3(a)	Amended and Restated Trust Agreement among Resource Capital Corp., Wells Fargo Bank, N.A., Wells Fargo Delaware Trust Company and the Administrative Trustees named therein, dated May 25, 2006. (2)
4.3(b)	Amendment to Amended and Restated Trust Agreement and Preferred Securities Certificate among Resource Capital Corp., Wells Fargo Bank, N.A. and the Administrative Trustees named therein, dated October 26, 2009 and effective September 30, 2009. (6)
4.4	Amended Junior Subordinated Note due 2036 in the principal amount of \$25,774,000, dated October 26, 2009. (6)
4.5(a)	Junior Subordinated Indenture between Resource Capital Corp. and Wells Fargo Bank, N.A., dated September 29, 2006. (3)
4.5(b)	Amendment to Junior Subordinated Indenture and Junior Subordinated Note due 2036 between Resource Capital Corp. and Wells Fargo Bank, N.A., dated October 26, 2009 and effective September 30, 2009. (6)
4.6(a)	Amended and Restated Trust Agreement among Resource Capital Corp., Wells Fargo Bank, N.A., Wells Fargo Delaware Trust Company and the Administrative Trustees named therein, dated September 29, 2006. (3)
4.6(b)	Amendment to Amended and Restated Trust Agreement and Preferred Securities Certificate among Resource Capital Corp., Wells Fargo Bank, N.A. and the Administrative Trustees named therein, dated October 26, 2009 and effective September 30, 2009. (6)
4.7	Amended Junior Subordinated Note due 2036 in the principal amount of \$25,774,000, dated October 26, 2009. (6)
10.1(a)	Amended and Restated Management Agreement between Resource Capital Corp., Resource Capital Manager, Inc. and Resource America, Inc. dated as of June 30, 2008. (4)
10.1(b)	First Amendment to Amended and Restated Management Agreement between Resource Capital Corp., Resource Capital Manager, Inc. and Resource America, Inc. dated as of June 30, 2008. (5)
10.1(c)	Second Amendment to Amended and Restated Management Agreement between Resource Capital Corp., Resource Capital Manager, Inc. and Resource America, Inc. dated as of August 17, 2010. (8)
10.1(d)	Third Amendment to Amended and Restated Management Agreement between Resource Capital Corp., Resource Capital Manager, Inc. and Resource America, Inc., dated February 24, 2011. (11)
10.2	

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Transfer and Contribution Agreement by and among LEAF Financial Corporation, Resource TRS, Inc., Resource Capital Corp. and LEAF Commercial Capital, Inc. dated January 4, 2011. (9)

10.3(a) Master Repurchase and Securities Contract by and among RCC Commercial, Inc., RCC Real Estate Inc. and Wells Fargo Bank, National Association, dated February 1, 2011. (10)

10.3(b) Guarantee Agreement made by Resource Capital Corp. in favor of Wells Fargo Bank, National Association, dated February 1, 2011. (10)

10.4 2005 Stock Incentive Plan. (1)

10.5 2007 Omnibus Equity Compensation Plan. (7)

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10.6(a)	Purchase Agreement by and between Churchill Financial Holdings, LLC and Resource TRS II, Inc., dated February 11, 2011.
10.6(b)	Guaranty by Resource Capital Corp., as guarantor, dated February 11, 2011.
31.1	Rule 13a-14(a)/Rule 15d-14(a) Certification of Chief Executive Officer.
31.2	Rule 13a-14(a)/Rule 15d-14(a) Certification of Chief Financial Officer.
32.1	Certification Pursuant to 18 U.S.C. Section 1350.
32.2	Certification Pursuant to 18 U.S.C. Section 1350.

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- (1) Filed previously as an exhibit to the Company's registration statement on Form S-11, Registration No. 333-126517.
  - (2) Filed previously as an exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.
  - (3) Filed previously as an exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2006.
    - (4) Filed previously as an exhibit to the Company's Current Report on Form 8-K filed on July 3, 2008.
    - (5) Filed previously as an exhibit to the Company's Current Report on Form 8-K filed on October 20, 2009.
  - (6) Filed previously as an exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2009.
  - (7) Filed previously as an exhibit to the Company's Annual Report on Form 10-K for the year ended December 31, 2008.
    - (8) Filed previously as an exhibit to the Company's Current Report on Form 8-K filed on August 19, 2010.
    - (9) Filed previously as an exhibit to the Company's Current Report on Form 8-K filed on January 6, 2011.
  - (10) Filed previously as an exhibit to the Company's Annual Report on Form 10-K for the year ended December 31, 2010.
    - (11) Filed previously as an exhibit to the Company's Current Report on Form 8-K filed on March 2, 2011.

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SIGNATURES

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

RESOURCE CAPITAL CORP.  
(Registrant)

Date: May 10, 2011

By: /s/ Jonathan Z. Cohen  
Jonathan Z. Cohen  
Chief Executive Officer and President

Date: May 10, 2011

By: /s/ David J. Bryant  
David J. Bryant  
Chief Financial Officer and Chief Accounting Officer

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