Table of Contents

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

FORM 10-Q

(Mark One);

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

For the quarterly period ended June 30, 2010

OR

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

For the transition period from _______ to _______.

Commission File Number 1-13610

PMC COMMERCIAL TRUST

(Exact name of registrant as specified in its charter)

TEXAS	75-6446078
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
17950 Preston Road, Suite 600, Dallas, TX 75252	(972) 349-3200
(Address of principal executive offices)	(Registrant's telephone number)

Indicate by check mark whether the Registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. YES o NO ☑

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 o

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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). YES o NO o

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

Large accelerated filer o	Accelerated filer ☑	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

As of August 3, 2010, the Registrant had outstanding 10,558,054 Common Shares of Beneficial Interest, par value $.01 per share.

PMC COMMERCIAL TRUST AND SUBSIDIARIES

INDEX

	PAGE NO.
PART I. Financial Information	
Item 1. Financial Statements	
Consolidated Balance Sheets *(Unaudited)* — June 30, 2010 and December 31, 2009	2
Consolidated Statements of Income *(Unaudited)* — Three and Six Months Ended June 30, 2010 and 2009	3
Consolidated Statements of Comprehensive Income *(Unaudited)* — Three and Six Months Ended June 30, 2010 and 2009	4
Consolidated Statements of Equity *(Unaudited)* — Three and Six Months Ended June 30, 2010 and 2009	5
Consolidated Statements of Cash Flows *(Unaudited)* — Six Months Ended June 30, 2010 and 2009	6
Notes to Consolidated Financial Statements *(Unaudited)*	7
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	21
Item 3. Quantitative and Qualitative Disclosures About Market Risk	40
Item 4. Controls and Procedures	44
PART II. Other Information	
Item 1. Legal Proceedings	45
Item 1A. Risk Factors	45
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	45
Item 3. Defaults upon Senior Securities	45
Item 4. Reserved	45
Item 5. Other Information	45
Item 6. Exhibits	46

Exhibit 31.1
Exhibit 31.2
Exhibit 32.1
Exhibit 32.2

PART I

Financial Information

ITEM 1.

Financial Statements

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

	June 30, 2010	December 31, 2009
	(Unaudited)	
ASSETS		
Loans receivable, net	$ 237,882	$ 196,642
Cash and cash equivalents	6,409	7,838
Restricted cash and cash equivalents	5,166	1,365
Real estate owned	2,223	5,479
Retained interests in transferred assets	901	12,527
Other assets	4,791	4,392
Total assets	$ 257,372	$ 228,243
LIABILITIES AND EQUITY		
Liabilities:		
Junior subordinated notes	$ 27,070	$ 27,070
Structured notes payable	25,272	8,291
Revolving credit facility	18,900	23,000
Secured borrowings — government guaranteed loans	17,628	—
Debentures payable	8,175	8,173
Borrower advances	3,394	2,368
Accounts payable and accrued expenses	2,527	2,364
Dividends payable	1,712	1,731
Deferred income	685	686
Redeemable preferred stock of subsidiary	—	1,975
Other liabilities	112	127
Total liabilities	105,475	75,785
Commitments and contingencies		
Beneficiaries' equity:		
Common shares of beneficial interest; authorized 100,000,000 shares of $0.01 par value; 11,094,383 and 11,084,683 shares issued at June 30, 2010 and December 31, 2009, respectively, 10,558,054 and 10,548,354 shares outstanding at June 30, 2010 and December 31, 2009, respectively	111	111
Additional paid-in capital	152,710	152,611
Net unrealized appreciation of retained interests in transferred assets	76	325
Cumulative net income	170,653	167,686
Cumulative dividends	(167,652)	(164,274)
	155,898	156,459
Less: Treasury stock; at cost, 536,329 shares at June 30, 2010 and December 31, 2009	(4,901)	(4,901)
Total beneficiaries' equity	150,997	151,558
Noncontrolling interests — cumulative preferred stock of subsidiary	900	900
Total equity	151,897	152,458
Total liabilities and equity	$ 257,372	$ 228,243

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

Table of Contents

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

	Six Months Ended June 30,		Three Months Ended June 30,	
	2010	**2009**	**2010**	**2009**
		(Unaudited)		
Revenues:				
Interest income	$ 6,715	$ 5,636	$ 3,498	$ 2,785
Income from retained interests in transferred assets	75	1,697	34	781
Other income	600	530	403	306
Total revenues	7,390	7,863	3,935	3,872
Expenses:				
Interest	2,000	1,596	1,011	790
Salaries and related benefits	1,911	1,920	970	999
General and administrative	1,212	977	644	534
Permanent impairments on retained interests in transferred assets	—	77	—	17
Provision for (reduction of) loan losses, net	(98)	203	104	56
Total expenses	5,025	4,773	2,729	2,396
Income before income tax benefit and discontinued operations	2,365	3,090	1,206	1,476
Income tax benefit	128	50	20	68
Income from continuing operations	2,493	3,140	1,226	1,544
Discontinued operations	8	50	(3)	20
Net income	$ 2,501	$ 3,190	$ 1,223	$ 1,564
Weighted average shares outstanding:				
Basic	10,549	10,599	10,550	10,548
Diluted	10,565	10,599	10,566	10,548
Basic and diluted earnings per share:				
Income from continuing operations	$ 0.24	$ 0.30	$ 0.12	$ 0.15
Discontinued operations	—	—	—	—
Net income	$ 0.24	$ 0.30	$ 0.12	$ 0.15

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

Table of Contents

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

	Six Months Ended June 30,		Three Months Ended June 30,	
	2010	**2009**	**2010**	**2009**
		(Unaudited)		
Net income	$ 2,501	$ 3,190	$ 1,223	$ 1,564
Change in unrealized appreciation of retained interests in transferred assets:				
Net unrealized appreciation arising during period	20	182	49	80
Net realized gains included in net income	(4)	(43)	(1)	(28)
	16	139	48	52
Comprehensive income	$ 2,517	$ 3,329	$ 1,271	$ 1,616

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

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

Six Months Ended June 30, 2009
(Unaudited)

	Common Shares of Beneficial Interest Outstanding	Par Value	Additional Paid-in Capital	Net Unrealized Appreciation of Retained Interests in Transferred Assets	Cumulative Net Income	Cumulative Dividends	Treasury Stock	Cumulative Preferred Stock of Subsidiary	Total Equity
Balances, January 1, 2009	10,694,788	$ 111	$ 152,460	$ 620	$ 160,925	$ (156,829)	$ (3,825)	$ 900	$154,362
Net unrealized appreciation	—	—	—	139	—	—	—	—	139
Treasury shares, net	(164,834)	—	—	—	—	—	(1,076)	—	(1,076)
Share-based compensation expense	18,400	—	103	—	—	—	—	—	103
Dividends ($0.385 per share)	—	—	—	—	—	(4,069)	—	—	(4,069)
Net income	—	—	—	—	3,190	—	—	—	3,190
Balances, June 30, 2009	10,548,354	$ 111	$ 152,563	$ 759	$ 164,115	$ (160,898)	$ (4,901)	$ 900	$152,649

Six Months Ended June 30, 2010
(Unaudited)

	Common Shares of Beneficial Interest Outstanding	Par Value	Additional Paid-in Capital	Net Unrealized Appreciation of Retained Interests in Transferred Assets	Cumulative Net Income	Cumulative Dividends	Treasury Stock	Cumulative Preferred Stock of Subsidiary	Total Equity
Balances, January 1, 2010	10,548,354	$ 111	$ 152,611	$ 325	$ 167,686	$ (164,274)	$ (4,901)	$ 900	$152,458
Cumulative effect adjustment	—	—	—	(265)	466	—	—	—	201
Net unrealized appreciation	—	—	—	16	—	—	—	—	16
Share-based compensation expense	9,700	—	99	—	—	—	—	—	99
Dividends ($0.32 per share)	—	—	—	—	—	(3,377)	—	—	(3,377)
Net income	—	—	—	—	2,501	—	—	—	2,501
Balances, June 30, 2010	10,558,054	$ 111	$ 152,710	$ 76	$ 170,653	$ (167,652)	$ (4,901)	$ 900	$151,897

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

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

	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
	(Unaudited)	
Cash flows from operating activities:		
Net income	$ 2,501	$ 3,190
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation	9	13
Permanent impairments on retained interests in transferred assets	—	77
Gains on sales of real estate	(78)	(50)
Deferred income taxes	(502)	(109)
Provision for (reduction of) loan losses, net	(98)	203
Unrealized premium adjustment	1,082	156
Amortization and accretion, net	30	(223)
Share-based compensation	99	103
Capitalized loan origination costs	(183)	(85)
Loans funded, held for sale	(19,826)	(6,454)
Proceeds from sale of guaranteed loans	—	7,677
Principal collected on loans	64	—
Loan fees remitted, net	(37)	(17)
Change in operating assets and liabilities:		
Other assets	(81)	199
Borrower advances	1,026	(1,262)
Accounts payable and accrued expenses	249	(1,236)
Other liabilities	(28)	(19)
Net cash provided by (used in) operating activities	(15,773)	2,163
Cash flows from investing activities:		
Loans funded	(3,118)	(1,348)
Principal collected on loans	8,677	7,541
Principal collected on retained interests in transferred assets	109	143
Principal collected on mortgage-backed security of affiliate	—	22
Investment in retained interests in transferred assets	—	(338)
Proceeds from sales of real estate owned	2,291	—
Investment in restricted cash and cash equivalents, net	(404)	(1,313)
Net cash provided by investing activities	7,555	4,707
Cash flows from financing activities:		
Purchase of treasury shares	—	(1,076)
Proceeds from (repayment of) revolving credit facility, net	(4,100)	1,100
Payment of principal on structured notes payable	(2,289)	(260)
Proceeds from secured borrowings — government guaranteed loans	18,639	—
Payment of principal on secured borrowings — government guaranteed loans	(64)	—
Redemption of redeemable preferred stock of subsidiary	(2,000)	(2,000)
Payment of dividends	(3,397)	(6,295)
Net cash provided by (used in) financing activities	6,789	(8,531)
Net decrease in cash and cash equivalents	(1,429)	(1,661)
Cash and cash equivalents, beginning of year	7,838	10,606
Cash and cash equivalents, end of period	$ 6,409	$ 8,945

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

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

Note 1. Basis of Presentation:

The accompanying interim financial statements of PMC Commercial Trust ("PMC Commercial" or together with its wholly-owned subsidiaries, "we," "us" or "our") have not been audited by independent accountants. These consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statement presentation. In the opinion of management, the financial statements reflect all adjustments necessary to present a fair statement of our financial position at June 30, 2010 and results of operations for the three and six months ended June 30, 2010 and 2009. These adjustments are of a normal recurring nature. All material intercompany balances and transactions have been eliminated. The results for the three and six months ended June 30, 2010 are not necessarily indicative of future financial results. Therefore, these financial statements should be read in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2009.

Certain prior period amounts have been reclassified to conform to the current year presentation. These reclassifications had no effect on previously reported consolidated net income or cash flows.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect (1) the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and (2) the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates. Our most sensitive estimates involve the valuation of our real estate owned and determination of loan loss reserves.

At December 31, 2009, we had two off-balance sheet securitizations: PMC Joint Venture, L.P. 2000 (the "2000 Joint Venture") and PMC Capital L.P. 1998-1 (the "1998 Partnership"). Due to a change in accounting rules, these qualified special purpose entities were consolidated beginning January 1, 2010. We used the unpaid principal balance method to recognize the assets and liabilities of these securitizations. The following table summarizes the assets and liabilities of the 2000 Joint Venture and the 1998 Partnership (which represents a non-cash transaction) which were previously included as retained interests in transferred assets ("Retained Interests"):

	January 1, 2010
	(In thousands)
Loans receivable, net	$ 27,752
Restricted cash and cash equivalents	3,396
Other assets	168
Total assets	$ 31,316
Structured notes payable (1)	$ 19,524
Other liabilities	58
Total liabilities	$ 19,582

(1) Included $254 held by PMC Commercial which was eliminated in consolidation.

Note 2. Summary of Significant Accounting Policies:

Our significant accounting policies are included in our Annual Report on Form 10-K for the year ended December 31, 2009. The following additional policies relate to changes in accounting principles effective January 1, 2010:

Restricted Cash and Cash Equivalents

Represents the collection and cash reserve accounts required to be held on behalf of the structured noteholders as collateral pursuant to the transaction documents. Cash reserve accounts may be required to be used to repay the structured noteholders pursuant to the transaction documents.

Secured Borrowings — Government Guaranteed Loans

Secured borrowings — government guaranteed loans represents legally sold SBA 7(a) loans which are treated as secured borrowings either temporarily (if the loans were sold for cash premiums until any potential contingency period for having to refund the premium has expired) or permanently (if the loans were sold for excess spread or if the loans were sold for excess spread and a premium). Excess spread represents the difference between the interest rate paid to us from our borrowers and the rate we paid to the purchaser of the guaranteed portion of the loan and servicing costs. To the extent secured borrowings include cash premiums, these premiums will be recognized as income after a period of at least 90 days for the loans sold solely for a cash premium or amortized as a reduction to interest expense over the life of the loan using the interest method for loans sold for a premium and excess spread.

Note 3. Recently Issued Accounting Pronouncements:

ASC topic 860 (formerly Financial Accounting Standards Board (“FASB”) No. 166, “Accounting for Transfers of Financial Assets — amendment of FASB Statement No. 140”) was issued in June 2009. ASC 860 amended the accounting guidance for transfers of financial assets including (1) eliminating the concept of qualified special purpose entities for prospective securitizations, (2) a new unit of account definition that must be met for transfers of portions of financial assets to be eligible for sale accounting, (3) clarifications and changes to the derecognition criteria for a transfer to be accounted for as a sale, (4) a change to the amount of recognized gain or loss on a transfer of financial assets accounted for as a sale when beneficial interests are received by the transferor, and (5) extensive new disclosures. ASC 860 was effective for interim and annual reporting periods beginning after November 15, 2009. This standard affected our accounting for secondary market loan sale transactions beginning on January 1, 2010, the date we adopted the standard. At a minimum, any premium income to be recognized is deferred for a period of at least 90 days since the proceeds received from legally sold portions of loans are treated as secured borrowings until any potential contingency period for having to refund the premiums is satisfied. Upon satisfaction of the contractual contingency period, both the unpaid principal balance of the guaranteed portion of the loan and the unamortized balance of the net secured borrowing will be derecognized, with the resulting gain on sale recorded in the income statement in the period when the contingencies are satisfied. Furthermore, to the extent certain criteria are not met, we are required to permanently treat certain of the proceeds received from legally sold portions of loans (those sold for excess spread or those sold for a cash premium and excess spread) as secured borrowings for the life of the loan. For statement of cash flows purposes, proceeds received from the sale of the guaranteed portion of SBA 7(a) loans are now reflected as a financing activity; whereas previously these proceeds were reflected as operating activities.

ASC topic 810 (formerly FASB No. 167, “Amendments to FASB Interpretation No. 46(R)”) was issued in June 2009. ASC 810 required an entity to perform an analysis to determine whether the entity’s variable interest or interests give it a controlling financial interest in a variable interest entity. This analysis identifies the primary beneficiary of a variable interest entity that has both of the following characteristics: (1) the power to direct the activities of a variable interest entity that most significantly impact the entity’s economic performance and (2) the obligation to absorb the losses of the entity that could potentially be significant to the variable interest entity. ASC 810 was effective for interim and annual reporting periods beginning after November 15, 2009. Our off-balance sheet securitizations were consolidated beginning January 1, 2010, the date we adopted the standard. Determining the carrying amounts of the assets and liabilities of the securitizations was not practicable and the assets of the securitizations can only be used to settle obligations of the securitizations; thus, the unpaid principal balance method was used to recognize assets and liabilities of the securitizations. The difference of $466,000 between the net amounts added to our consolidated balance sheet as assets and liabilities and our Retained Interests was recognized as a cumulative effect adjustment in our beneficiaries’ equity. Unrealized appreciation of Retained Interests of $265,000 was reversed in conjunction with the consolidation; therefore, the net effect to our beneficiaries’ equity was an increase of $201,000.

ASC topic 310 was issued in July 2010. ASC 310 requires additional disclosures about the credit quality of financing receivables and the allowance for credit losses. ASC 310 is effective for interim and annual reporting periods ending on or after December 15, 2010. We are currently evaluating the effect of ASC 310 on our consolidated financial statements.

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

Note 4. Share-Based Compensation Plans:

We granted 26,500 option awards on June 12, 2010 at an exercise price of $8.35 (the closing price on June 11, 2010). The fair value of this option award was estimated at the date of grant using the Black-Scholes option-pricing model with the following assumptions:

Assumption	
Expected Term (years)	3.0
Risk-Free Interest Rate	1.23%
Expected Dividend Yield	7.66%
Expected Volatility	40.29%
Expected Forfeiture Rate	10.0%

The expected term of the options granted represents the period of time that the options are expected to be outstanding and was based on historical data. The risk-free rate was based on the three-year U.S. Treasury rate corresponding to the expected term of the options. We used historical information to determine our expected volatility and forfeiture rates. We recorded compensation expense of approximately $33,000 during the three and six months ended June 30, 2010 related to this option grant. We granted 15,000 option awards on June 13, 2009 at an exercise price of $8.35 (the closing price on June 12, 2009) and recorded compensation expense of approximately $11,000 during the three and six months ended June 30, 2009.

In addition, we issued an aggregate of 13,100 restricted shares to executive officers and our Board of Trust Managers on June 12, 2010 at the then current market price of the shares of $8.35. We issued an aggregate of 18,400 and 16,500 restricted shares to executive officers and our Board of Trust Managers on June 13, 2009 and June 14, 2008, respectively, at the then current market price of the shares. There were forfeitures of 3,400 restricted shares during June 2010. The restricted shares vest based on two years of continuous service with one-third of the shares vesting immediately upon issuance of the shares and one-third vesting at the end of each of the next two years. Restricted share awards provide for accelerated vesting if there is a change in control (as defined in the plan).

Compensation expense related to the restricted shares is being recognized over the vesting periods. We recorded compensation expense of $42,000 and $72,000 during the three months ended June 30, 2010 and 2009, respectively, and $66,000 and $92,000 during the six months ended June 30, 2010 and 2009, respectively, related to restricted shares. As of June 30, 2010, there was approximately $81,000 of total unrecognized compensation expense related to restricted shares which will be recognized over the next two years.

Table of Contents

Note 5. Loans Receivable, net:

Loans receivable, net, consisted of the following:

	June 30, 2010	December 31, 2009
	(In thousands)	
Commercial mortgage loans (1)	$ 176,389	$ 155,137
SBA 7(a) program loans (2)	35,346	15,256
SBIC commercial mortgage loans (3)	27,438	27,854
Total loans receivable	239,173	198,247
Less:		
Deferred commitment fees, net	(91)	(348)
Loan loss reserves	(1,200)	(1,257)
Loans receivable, net	$ 237,882	$ 196,642

(1) At June 30, 2010 and December 31, 2009, included approximately $17.9 million and $19.8 million of loans, respectively, held as collateral for the outstanding structured notes of PMC Joint Venture, L.P. 2003 (the "2003 Joint Venture"). At June 30, 2010, included approximately $26.1 million of loans held as collateral for the outstanding structured notes of the 2000 Joint Venture and the 1998 Partnership. The remaining loans are held as collateral for our revolving credit facility.

(2) Net of retained loan discounts of $1.4 million and $1.5 million at June 30, 2010 and December 31, 2009, respectively. At June 30, 2010, included approximately $16.6 million (guaranteed loan portion) of loans which were sold with the proceeds received from the sale reflected as secured borrowings — government guaranteed loans (a liability on our consolidated balance sheet).

(3) Originated by our Small Business Investment Company ("SBIC") subsidiaries.

The activity in our loan loss reserves was as follows:

	Six Months Ended June 30,	
	2010	2009
	(In thousands)	
Balance, beginning of year	$ 1,257	$ 480
Provision for loan losses	306	267
Reduction of loan losses	(404)	(64)
Consolidation of the 2000 Joint Venture and the 1998 Partnership reserves	184	—
Principal balances written-off	(143)	(11)
Balance, end of period	$ 1,200	$ 672

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

Information on those loans considered to be impaired loans (loans for which it is probable that the lender will be unable to collect all amounts due according to the original contractual terms of the loan) was as follows:

	June 30, 2010	December 31, 2009
	(In thousands)	
Impaired loans requiring reserves	$ 1,104	$ 3,132
Impaired loans expected to be fully recoverable	1,216	228
Total impaired loans	$ 2,320	$ 3,360

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
	(In thousands)			
Average impaired loans	$ 3,915	$ 7,582	$ 4,190	$ 6,456
Interest income on impaired loans	$ 57	$ 9	$ 71	$ 17

Note 6. Retained Interests:

Our Retained Interests consisted of the following:

	June 30, 2010		December 31, 2009	
	Estimated Fair Market Value	Cost	Estimated Fair Market Value	Cost
	(In thousands)			
First Western	$ 901	$ 825	$ 994	$ 934
1998 Partnership (1)	—	—	1,393	1,355
2000 Joint Venture (1)	—	—	10,140	9,913
	$ 901	$ 825	$ 12,527	$ 12,202

(1) Effective January 1, 2010, due to a change in accounting rules, we now consolidate the assets and liabilities of the 1998 Partnership and the 2000 Joint Venture.

The SBA guaranteed portions of the loans receivable are sold to either dealers in government guaranteed loans receivable or institutional investors ("Secondary Market Loan Sales") when each individual loan becomes fully funded. Our SBA 7(a) subsidiary has Retained Interests related to the sale of loans originated pursuant to the SBA 7(a) Program prior to January 1, 2010. Effective January 1, 2010, based on a change in accounting rules, we no longer record additions to Retained Interests.

On Secondary Market Loan Sales prior to January 1, 2010, to the extent we retained an excess spread between the interest rate paid to us from our borrowers and the rate we paid to the purchaser of the guaranteed portion of the note and the required minimum servicing spread, we established Retained Interests. In determining the estimated fair value of our Retained Interests related to Secondary Market Loan Sales completed prior to January 1, 2010, our assumptions at June 30, 2010 included a prepayment speed of 20% per annum and a discount rate of 14%.

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

The following sensitivity analysis of our Retained Interests at June 30, 2010 highlights the volatility that results when prepayments and discount rates are different than our assumptions:

Changed Assumption	Estimated Fair Value	Asset Change (1)
	(In thousands)	
Prepayments increase by 500 basis points per annum	$ 797	($104)
Prepayments increase by 1000 basis points per annum	$ 716	($185)
Discount rates increase by 300 basis points	$ 846	($55)
Discount rates increase by 500 basis points	$ 813	($88)

(1) Any depreciation of our Retained Interests would be either included in the accompanying statement of income as a permanent impairment or on our consolidated balance sheet in beneficiaries' equity as an unrealized loss.

No credit losses are assumed for our Retained Interests since the SBA has guaranteed the payment of the principal on these loans.

These sensitivities are hypothetical and should be used with caution. Values based on changes in these assumptions generally cannot be extrapolated since the relationship of the change in assumptions to the change in estimated fair value is not linear. The effect of a variation in a particular assumption on the estimated fair value of our Retained Interests is calculated without changing any other assumption. In reality, changes in one factor are not isolated from changes in another which might magnify or counteract the sensitivities.

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

Note 7. Debt:

Information on our debt was as follows:

	Carrying Value (1)		Weighted Average Coupon Rate at		Weighted Average Interest Rate on Underlying Loans at
	June 30, 2010	December 31, 2009	June 30, 2010	December 31, 2009	June 30, 2010
	(Dollars in thousands, except footnotes)				
Structured notes payable (2):					
2003 Joint Venture	$ 7,701	$ 8,291	2.79%	2.79%	4.29%(3)
2000 Joint Venture	14,031	—	7.28%	NA	9.49%
1998 Partnership	3,540	—	2.25%	NA	4.97%
	25,272	8,291			
Junior subordinated notes	27,070	27,070	3.54%	3.53%	NA
Revolving credit facility	18,900	23,000	3.25%	3.25%	NA
Debentures payable	8,175	8,173	5.90%	5.90%	NA
Secured borrowings — government guaranteed loans (4):					
Loans sold for premiums	5,816	—	4.52%	NA	5.97%
Loans sold for a premium and excess spread	5,846	—	4.03%	NA	6.00%
Loans sold for excess spread	5,966	—	1.59%	NA	5.96%
	17,628	—			
Redeemable preferred stock of subsidiary (5)	—	1,975	NA	4.00%	NA
Debt	$ 97,045	$ 68,509			

(1) *The face amount of debt as of June 30, 2010 and December 31, 2009 was $97,060,000 and $68,551,000, respectively.*

(2) *Beginning January 2010, due to a change in accounting rules, the 2000 Joint Venture and the 1998 Partnership were consolidated.*

(3) *The weighted average rate on the underlying collateral for the 2003 Joint Venture at December 31, 2009 was 4.31%.*

(4) *Due to a change in accounting rules, effective January 1, 2010, cash proceeds received from government guaranteed loans sold for (1) premiums are reflected temporarily as secured borrowings until any potential contingency period for having to refund the premiums is satisfied, (2) excess spread are reflected permanently as secured borrowings for the life of the loan and (3) premiums and excess spread are reflected permanently as secured borrowings for the life of the loan (principal portion) and temporarily as secured borrowings until any potential contingency period for having to refund the premiums is satisfied (for cash premiums) and then amortized as a reduction of interest expense over the life of the loan. For loans sold for premiums, the spread is 1%; however, the weighted average coupon rate reflects an adjustment for the cash premium received. For loans sold for premiums and excess spread, the weighted average coupon rate reflects an adjustment for the cash premium received.*

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

(5) *During March 2010, we redeemed 20,000 shares of $100 par value, 4% cumulative preferred stock of one of our SBICs held by the SBA due in May 2010. No gain or loss was recorded on the redemption.*

Principal payments on our debt at June 30, 2010 were as follows:

Years Ending June 30,	Total	Structured Notes and Secured Borrowings (1)	All Other Debt (2)
		(In thousands)	
2011	$ 28,668	$ 9,768	$ 18,900
2012	4,230	4,230	—
2013	4,546	4,546	—
2014	8,675	4,485	4,190
2015	8,579	4,579	4,000
Thereafter	42,362	15,292	27,070
	$ 97,060	$ 42,900	$ 54,160

(1) *Principal payments are generally dependent upon cash flows received from the underlying loans. Our estimate of their repayment is based on scheduled principal payments on the underlying loans. Our estimate will differ from actual amounts to the extent we experience prepayments and/or loan losses. In addition, secured borrowings — loans sold for premiums are treated as current due to the potential contingency period expiring within approximately 90 days.*

(2) *Represents the revolving credit facility, junior subordinated notes and debentures payable.*

Note 8. Earnings Per Share:

The computations of basic earnings per common share are based on our weighted average shares outstanding. For purposes of calculating diluted earnings per share, the weighted average shares outstanding were increased by 16,000 shares during both the three and six months ended June 30, 2010. During the three and six months ended June 30, 2009, no shares were added to the weighted average shares outstanding for purposes of calculating diluted earnings per share as options were anti-dilutive.

Not included in the computation of diluted earnings per share were outstanding options to purchase approximately 77,000 and 90,000 common shares during the three and six months ended June 30, 2010 and 2009, respectively, because the options' exercise prices were greater than the average market price of the shares.

Note 9. Dividends Declared:

Dividends declared during 2010 were as follows:

Date Paid	Record Date	Amount Per Share
April 12, 2010	March 31, 2010	$ 0.16
July 12, 2010	June 30, 2010	0.16
		$ 0.32

We have certain covenants within our revolving credit facility which limit our ability to pay out returns of capital as part of our dividends. These restrictions have not historically limited the amount of dividends we have paid and management does not believe that they will restrict future dividend payments.

Note 10. Income Taxes:

PMC Commercial has elected to be taxed as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended (the "Code"). To qualify as a REIT, PMC Commercial must meet a number of organizational and operational requirements, including a requirement that we distribute at least 90% of our REIT taxable income to our shareholders. As a REIT, PMC Commercial generally will not be subject to corporate level Federal income tax on net income that is currently distributed to shareholders. In order to meet our 2009 taxable income distribution requirements, we will make an election under the Code to treat a portion of the distributions declared in 2010 as distributions of 2009's REIT taxable income.

PMC Commercial has wholly-owned taxable REIT subsidiaries ("TRS's") which are subject to Federal income taxes. The income generated from the TRS's is taxed at normal corporate rates.

Note 11. Fair Value Measurements:

At June 30, 2010, Retained Interests was our only asset that was required to be measured at fair value on a recurring basis. No liabilities were required to be measured at fair value on a recurring basis. A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. In general, quoted market prices from active markets for the identical asset (Level 1 inputs), if available, should be used to value an asset. If quoted prices are not available for the identical asset, then a determination should be made if Level 2 inputs are available. Level 2 inputs include quoted prices for similar assets in active markets or for identical or similar assets in markets that are not active (*i.e.*, markets in which there are few transactions for the asset, the prices are not current, price quotations vary substantially, or in which little information is released publicly). There is little or no market information for our Retained Interests, thus there are no Level 1 or Level 2 determinations available. Level 3 inputs are unobservable inputs for the asset. Unobservable inputs are used to measure fair value when observable inputs are not available. These inputs include our expectations about the assumptions that market participants would use in pricing the asset in a current transaction.

Table of Contents

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

We use Level 3 inputs to determine the estimated fair value of our Retained Interests. The following is activity for our Retained Interests:

	Six Months Ended June 30,	
	2010	2009
	(In thousands)	
Value, beginning of period	$ 12,527	$ 33,248
Principal collections	(109)	(143)
Realized gains included in net income (1)	(4)	(43)
Investments	—	556
Permanent impairments	—	(77)
Consolidation (2)	(11,734)	(8,565)
Cumulative effect adjustment (3)	201	—
Accretion (4)	—	241
Unrealized appreciation	20	182
Value, end of period	$ 901	$ 25,399
Cost, end of period	$ 825	$ 24,640

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(1) *Included within income from Retained Interests.*

(2) *During the six months ended June 30, 2010, represents the consolidation of the 2000 Joint Venture and the 1998 Partnership based upon new accounting rules effective January 1, 2010. During the six months ended June 30, 2009, represents the consolidation of a securitization which attained its "clean-up" call provision.*

(3) *Based on a change in accounting rules, we consolidated the 2000 Joint Venture and the 1998 Partnership effective January 1, 2010. The difference of $466,000 between the amounts added to our consolidated balance sheet as assets and liabilities and our Retained Interests was recognized as a cumulative effect adjustment in our beneficiaries' equity. Unrealized appreciation of Retained Interests of $265,000 was reversed in conjunction with the consolidation; therefore, the net effect to our beneficiaries' equity was an increase of $201,000.*

(4) *Represents accretion of income in excess of principal collections, included within income from Retained Interests.*

We may be required, from time to time, to measure certain other assets at fair value on a nonrecurring basis. These adjustments to fair value usually result in the recognition of loan loss reserves on individual loans and valuation reserves on real estate owned based on the estimated fair value.

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

For impaired loans measured at fair value on a nonrecurring basis during the six months ended June 30, 2010 and 2009, the following table provides the carrying value of the related individual assets at quarter end. We used Level 3 inputs to determine the estimated fair value of our impaired loans.

	Carrying Value at June 30,		Provision for Loan Losses Six Months Ended June 30, (2)	
	2010	2009	2010	2009
	(In thousands)			
Impaired loans (1)	$ 2,053	$ 7,961	$ 101	$ 173

(1) *Carrying value represents our impaired loans net of loan loss reserves. Our carrying value is determined based on management's assessment of the fair value of the collateral based on numerous factors including operating statistics to the extent available, appraised value of the collateral, tax assessed value and market environment.*

(2) *Represents the net change in the provision for loan losses included in our consolidated statements of income related specifically to these loans during the periods presented.*

For real estate owned, our carrying value approximates the estimated fair value at the time of foreclosure and the lower of cost or fair value thereafter. We use Level 3 inputs to determine the estimated fair value of our real estate owned. The carrying value of our real estate owned is established at the time of foreclosure based upon management's assessment of its fair value based on numerous factors including operating statistics to the extent available, the appraised value, tax assessed value and market environment. At June 30, 2010, the carrying value and estimated fair value of our real estate owned was $2,223,000.

The estimated fair values of our financial and nonfinancial instruments were as follows at June 30, 2010:

	Carrying Amount	Estimated Fair Value
	(In thousands)	
Assets:		
Loans receivable, net	$ 237,882	$ 232,329
Retained Interests	901	901
Restricted cash and cash equivalents	5,166	5,166
Cash and cash equivalents	6,409	6,409
Liabilities:		
Structured notes payable	25,272	25,249
Secured borrowings — government guaranteed loans	17,628	16,569
Debentures payable	8,175	8,886
Revolving credit facility	18,900	18,900
Junior subordinated notes	27,070	16,612

In general, estimates of fair value may differ from the carrying amounts of the financial assets and liabilities primarily as a result of the effects of discounting future cash flows. Considerable judgment is required to interpret market data and develop estimates of fair value. Accordingly, the estimates presented may not be indicative of the amounts we could realize in a current market exchange.

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

Loans receivable, net: Our loans receivable are recorded at cost and adjusted by net loan origination fees and discounts. In order to determine the estimated fair value of our loans receivable, we use a present value technique for the anticipated future cash flows using certain assumptions including a current discount rate, prepayment tendencies and potential loan losses. Reserves are established based on numerous factors including, but not limited to, the creditor's payment history, collateral value, guarantor support and other factors. In the absence of a readily ascertainable market value, the estimated value of our loans receivable may differ from the values that would be placed on the portfolio if a ready market for the loans receivable existed.

Retained Interests: In order to determine the estimated fair value of our Retained Interests, we use a present value technique for the anticipated future cash flows using certain assumptions including a current discount rate and prepayment tendencies.

Restricted cash and cash equivalents: Restricted cash and cash equivalents represent our collection and reserve accounts of the securitizations. The carrying amount is considered to be a reasonable estimate of their fair value due to (1) the short maturity of the collection account and (2) the reserve accounts providing collateral value at their current carrying amounts to the structured noteholders.

Cash and cash equivalents: The carrying amount is considered to be reasonable estimates of fair value due to the short maturity of these funds.

Structured notes payable, debentures payable and junior subordinated notes: The estimated fair value is based on a present value calculation based on prices of the same or similar instruments after considering market risks, current interest rates and remaining maturities.

Secured borrowings — government guaranteed loans: The estimated fair value approximates cost, adjusted for cash premiums, as the loans were sold in current third-party transactions.

Revolving credit facility: The carrying amount is a reasonable estimation of fair value as the interest rate on this instrument is variable and the short duration to maturity.

Note 12. Supplemental Disclosure of Cash Flow Information:

Information regarding our non-cash activities was as follows:

	Six Months Ended June 30,	
	2010	2009
	(In thousands)	
Loans receivable reclassified to real estate owned	$ 2,380	$ —
Reclassification from secured borrowings — government guaranteed loans to loans receivable, net	$ 2,007	$ —
Loans receivable originated to facilitate sales of real estate owned	$ 3,325	$ —
Consolidation of loans receivable	$ —	$ 12,570

In addition, as described in Note 1, effective January 1, 2010, we are now consolidating the assets and liabilities of the 2000 Joint Venture and the 1998 Partnership, representing non-cash transactions. Previously, the 2000 Joint Venture and the 1998 Partnership were reflected as Retained Interests.

Note 13. Commitments and Contingencies:

Loan Commitments

Commitments to extend credit are agreements to lend to a customer provided the terms established in the contract are met. Our outstanding loan commitments and approvals to fund loans were approximately $9.5 million at June 30, 2010, the majority of which were for prime-based loans to be originated by First Western, the government guaranteed portion of which is intended to be sold. Commitments generally have fixed expiration dates. Since some commitments are expected to expire without being drawn upon, total commitment amounts do not necessarily represent future cash requirements.

Operating Lease

We lease office space in Dallas, Texas under a lease which expires in October 2011. Future minimum lease payments under this lease approximate $295,000.

Employment Agreements

We have employment agreements with our executive officers for three-year terms expiring June 30, 2013. Under certain circumstances, as defined within the agreements, the agreements provide for severance compensation to the executive officer in a lump sum payment in an amount equal to 2.99 times the average of the last three years annual compensation paid to the executive officer.

Structured Loan Sale Transactions

The documents of the structured loan sale transactions contain provisions (the “Credit Enhancement Provisions”) that govern the assets and the inflow and outflow of funds of the entities originally formed as part of the structured loan sale transactions. The Credit Enhancement Provisions include specified increased reserve requirements. If, at any measurement date, the loans in structured loan transactions were delinquent in excess of specified limits or were considered “charged-off” loans in accordance with the transaction documents, the Credit Enhancement Provisions would require an increase in the level of credit enhancement (reserve fund). During the period in which the Credit Enhancement Provisions were in effect, excess cash flow from the entity, if any, which would otherwise be distributable to us, would be used to fund the increased credit enhancement levels until the specified reserve requirement was met and would delay or reduce our distribution. In general, there can be no assurance that amounts deferred under Credit Enhancement Provisions would be received in future periods or that future deferrals or losses would not occur. As a result of a delinquent loan in the 2003 Joint Venture, Credit Enhancement Provisions were triggered during the first quarter of 2009. As a consequence, cash flows related to this transaction otherwise distributable to us are being deferred and utilized to fund the increased credit enhancement requirement. Based on current cash flow assumptions, management anticipates that the funds will be received in future periods or used to repay the structured notes to the extent we exercise the “clean-up” call option.

Litigation

We had significant outstanding claims against Arlington Hospitality, Inc.’s and its subsidiary, Arlington Inns, Inc.’s (together “Arlington”) bankruptcy estates. Arlington objected to our claims and initiated a complaint in the bankruptcy seeking, among other things, the return of payments Arlington made pursuant to the property leases and the master lease agreement. While confident that a substantial portion of our claims would have been allowed and the claims against us would have been disallowed, due to the exorbitant cost of defense coupled with the likelihood of reduced available assets in the debtors’ estates to pay claims, we executed an agreement with Arlington to settle our claims against Arlington and Arlington’s claims against us. The settlement provides that Arlington will dismiss its claims seeking the return of certain payments made pursuant to the property leases and master lease agreement and substantially reduces our claims against the Arlington estates. The settlement further provides for mutual releases among the parties. The Bankruptcy Court approved the settlement. Accordingly, there are no remaining assets or liabilities recorded in the accompanying consolidated financial statements related to this matter. However, the settlement will only become final upon the Bankruptcy Court’s approval of Arlington’s liquidation plan which was filed during the third quarter of 2007. Due to the complexity of the bankruptcy, we cannot estimate when, or if, the liquidation plan will be approved.

In the normal course of business we are periodically party to certain legal actions and proceedings involving matters that are generally incidental to our business (*i.e.*, collection of loans receivable). In management’s opinion, the resolution of these legal actions and proceedings will not have a material adverse effect on our consolidated financial statements.

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

Other

We provide standard representations and warranties to the SBA at the time we sell the guaranteed portion of the loan. If the SBA establishes that a loss on an SBA guaranteed loan is attributable to significant technical deficiencies (a breach of standard representations and warranties) in the manner in which the loan was originated, funded or serviced by First Western, the SBA may seek recovery of funds from us. With respect to the guaranteed portion of SBA loans that have been sold, the SBA will first honor its guarantee and then seek compensation from us in the event that a loss is deemed to be attributable to technical deficiencies.

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

This Form 10-Q contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which are intended to be covered by the safe harbors created thereby. Such forward-looking statements can be identified by the use of forward-looking terminology such as "may," "will," "expect," "intend," "believe," "anticipate," "estimate," or "continue," or the negative thereof or other variations or similar words or phrases. These statements include the plans and objectives of management for future operations, including, but not limited to, plans and objectives relating to future growth of the loan portfolio and availability of funds. The forward-looking statements included herein are based on current expectations and there can be no assurance that these expectations will be attained. Assumptions relating to the foregoing involve judgments with respect to, among other things, future economic, competitive and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond our control. Although we believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could be inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this Form 10-Q will prove to be accurate. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that our objectives and plans will be achieved. Readers are cautioned not to place undue reliance on forward-looking statements. Forward-looking statements speak only as of the date they are made. We do not undertake to update them to reflect changes that occur after the date they are made.

The following discussion of our financial condition at June 30, 2010 and results of operations for the three and six months ended June 30, 2010 and 2009 should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2009. For a more detailed description of the risks affecting our financial condition and results of operations, see "Risk Factors" in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2009.

EXECUTIVE SUMMARY

Liquidity

Our revolving credit facility (the "Revolver"), which is collateralized by PMC Commercial's loans, matures on December 31, 2010. The amount available under the Revolver is currently $30 million and reduces to $25 million on October 1, 2010. Upon maturity the amount available will be $20 million. We are currently addressing the extension of our facility for an additional year with our lender.

During the first half of 2010, we were able to reduce the outstanding balance under our Revolver by $4.1 million while our capital outlay to fund loans was $22.9 million. We received $18.6 million in proceeds from selling the government guaranteed portion of loans, $5.7 million in principal from payments on our loans receivable that collateralize our Revolver and $2.3 million in proceeds from selling real estate owned.

Our net capital outlay for loans during the second half of 2010 (loans to be funded less proceeds from loans to be sold) is anticipated to be approximately $4.0 million. Our anticipated scheduled principal payments on our loan portfolio during the second half of 2010 are $3.0 million which would be available to repay a portion of the existing balance under the Revolver. Based on the above cash activity and other factors, we currently anticipate that the balance outstanding under our Revolver will be approximately $20.0 million, without any proceeds from loan principal prepayments or cash sales of real estate owned or alternatively, any unforeseen uses of funds.

For 2011, we will need funds to originate loans. To the extent the maximum guarantees under the SBA 7(a) Program are capped at 75%, we anticipate that we would need between $7.5 million and $10.0 million in 2011 to fund our SBA 7(a) anticipated gross fundings of between $30.0 million and $40.0 million. Our anticipated scheduled principal payments on our loan portfolio in 2011 are $6.0 million which would be available to repay a portion of any balance under the Revolver. Accordingly, without any loan principal prepayments, we would need additional borrowing capacity of between $1.5 million and $4.0 million. This analysis does not take into account potential additional working capital needs such as (1) timing differences between when we originate a loan and when we receive the proceeds from the sold loan, (2) continuation of a cash dividend that exceeds our cash generated from operations, (3) outlay of funds needed to protect our loans receivable during the foreclosure process or (4) unforeseen cash needs.

We believe that we will be able to get the liquidity to fund our loans in 2011 by extending and increasing our Revolver to between $25.0 million and $30.0 million and through funds provided by principal prepayments on our loans. To the extent we are unable to extend or increase our Revolver, we may have to reduce the level of loan originations in 2011.

General Economic Environment

There has been an increase in mortgage defaults in the broader commercial real estate market and a belief that these defaults may increase. This increase is due in part to credit market turmoil and declining property cash flows and property values. In addition, when there are more foreclosures on commercial real estate properties the property values typically decline even further as supply exceeds demand in the market for the properties underlying these mortgages. We have experienced an increase in foreclosure activity. In conjunction with this increase in foreclosure activity, we have experienced, and will likely continue to experience, an increase in expenses as costs associated with these properties are incurred. In addition, we may experience an increase in loan losses and/or impairment losses. Further, our ability to sell our real estate owned will be affected by many factors, including but not limited to, the number of potential buyers, number of competing properties on the market and other market conditions.

Market Conditions

As a result of the current business environment including depressed real estate markets, liquidity has been severely restricted. Capital providers (including banks and insurance companies) substantially reduced the availability and increased the cost of debt capital for many companies originating commercial mortgages. We are uncertain as to how long the present economic conditions will remain and what shape the economy will take.

In response, legislators and financial regulators implemented a number of mechanisms designed to add stability to the financial markets. These programs and other legislative and regulatory efforts related to the financial markets provided increased liquidity to global financial markets. However, many of the government sponsored programs were temporary or have been completely utilized. The expiration of these or other legislative or regulatory initiatives may cause a further reduction in liquidity to the financial markets and as a result, we may need to modify our strategies, businesses or operations, and incur increased costs in order to satisfy new regulatory requirements or to compete in a changing business environment. Given the volatile nature of the market and uncertainties underlying efforts to mitigate or reverse the disruption, we may not timely anticipate or manage existing, new or additional risks, contingencies or developments. Our failure to do so could materially and adversely affect our business, financial condition, results of operations and prospects.

We rely on the market for Secondary Market Loan Sales. This market may diminish and/or the premiums achieved on selling loans into that market may be reduced which could have a material adverse effect on our ability to originate new loans.

Strategic Alternatives

The current credit and capital market environment remains unstable. While we continue to explore and evaluate strategic opportunities, our primary focus is on maximizing the value of our current investment portfolio and business strategy as well as exploring opportunities for alternative liquidity sources.

SBA 7(a) Program and Regulatory Environment

As a result of reduced liquidity, we continue to focus on the origination of SBA 7(a) Program loans which require less capital due to the ability to sell the government guaranteed portion of such loans. We utilize the SBA 7(a) Program to originate small business loans and then sell the government guaranteed portion to investors.

The American Recovery and Reinvestment Act (the "Stimulus Bill"), passed in February 2009, contained provisions that benefitted the SBA which we believe had a positive impact on our lending operations. The Stimulus Bill provided the SBA with temporary funding to eliminate fees on SBA 7(a) Program loans and provided increased SBA guarantee percentages on SBA 7(a) Program loans of up to 90% for certain loans during periods of time all of which ended before May 31, 2010. There is currently legislation being reviewed by Congress that contains provisions to allow the SBA to support larger loans and provide more financing options to a larger segment of small businesses including (1) increasing the 7(a) loan limit from $2 million to $5 million, (2) allowing the 504 loan program to refinance short-term commercial real estate debt into long-term, fixed-rate loans and (3) extending the authorization to provide 90% guarantees on 7(a) loans and fee elimination for borrowers on 7(a) and 504 loans through December 31, 2010. We believe that we would benefit from the increase in 7(a) loan limits, extension of 90% guarantees on 7(a) loans and fee elimination for borrowers on 7(a) loans. We are not currently utilizing the 504 program due to our limited liquidity.

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Act"), passed in July 2010, provides new regulations and oversight of the financial services industry. We do not believe that this Act will have a material impact on us.

Secondary Market Loan Sales

During the first half of 2010, we sold $18.6 million of the guaranteed portion of SBA 7(a) Program loans. Loans were sold for (1) cash premiums and a benefit of 100 basis points (1%) (the minimum spread required to be retained pursuant to SBA regulations) for a servicing spread on the sold portion of the loan, (2) future servicing spreads averaging 437 basis points (including the 100 basis points required to be retained) and no cash premiums, or (3) future servicing spreads averaging 156 basis points (including the 100 basis points required to be retained) and cash premiums of 10% (*i.e.*, "hybrid loan sales"). As a result of the new accounting rules regarding sale treatment for selling the guaranteed portion of our SBA 7(a) Program loans, no gain is recognized at the time of sale for any of these loan sales.

For the loan sales where we received cash premiums and the minimum servicing spread of 1%, sale treatment will occur after any contingencies have been satisfied which should occur 90 to 120 days after the proceeds were received. We recorded $204,000 (before cost allocations) in gains on sale during the second quarter of 2010 relating to these loans sales in the first quarter of 2010 (reflected as premium income included in other income in our consolidated income statements). We expect to record a gain from sale of $570,000 (before cost allocations) during the third quarter of 2010 relating to these loan sales in the second quarter of 2010. Once gains are recorded, there is no significant difference between the old and new accounting rules for these sales. In effect, the change in the accounting rules is to defer gain recognition during the contingency period of at least 90 days.

The more significant accounting rule change relates to those loans where management believes the best economic opportunity was to forego the up-front cash premiums in lieu of significant future servicing spread or to sell the loan for an up-front cash premium and lesser future servicing spread (than if the loan was sold solely for future servicing spread). On these loan sales, we receive a spread between the rate we collect from our borrowers and the rate we pay the buyers of the guaranteed portion of the loan. For loans sold solely for excess spread, this spread includes the average excess spread of 337 basis points to be received in future periods in addition to the SBA mandated 100 basis points.

For tax purposes, since all of these transactions are legal sales, we are required to record gains based on present value cash flow techniques consistent with the book accounting treatment utilized until January 1, 2010.

Consequently, for tax purposes, we had gains of approximately $658,000 during the six months ended June 30, 2010 related to sales of loans solely for excess spread but will not recognize any gains for book purposes. Instead, we will record book income as we receive the average 437 basis point spread as we service the sold portion of the loan. There can be no assurance that the loans will remain outstanding until maturity. However, management believes that the discounted present value of the future servicing income will be greater than the cash premiums we would have received since we expect the life of the loans (and the future incremental cash flows) to exceed the foregone premiums.

In addition, for tax purposes, we had gains of approximately $629,000 during the six months ended June 30, 2010 related to sales of loans for a cash premium and excess spread but will not recognize gain for book purposes. Upon expiration of the contingency period, the cash premium will be amortized as a reduction of interest expense over the life of the loan using the interest method. We will record book income as we receive the average 156 basis point excess spread as we service the sold portion of the loan.

The following highlights the difference between selling a loan for cash premium versus selling a loan for future excess spread versus selling a loan for a cash premium and future excess spread:

	Cash Premium	Excess Spread	Hybrid
Loan amount	$ 1,000,000	$ 1,000,000	$ 1,000,000
Guaranteed portion of total loan	90.00%	90.00%	90.00%
Guaranteed loan amount	$ 900,000	$ 900,000	$ 900,000
Rate paid by borrower	6.00%	6.00%	6.00%
Rate paid to purchaser	5.00%	1.75%	4.43%
Total spread on sold portion of loan	1.00%	4.25%	1.57%
Premium percentage	10.25%	—	10.00%
Proceeds from sale	$ 992,250	$ 900,000	$ 990,000
Premium received	$ 92,250	$ —	$ 90,000
Future servicing spread:			
Estimated cash flow — Year 1	$ 8,900	$ 37,900	$ 14,000
Estimated cash flow — Initial 5 years	$ 42,800	$ 182,200	$ 67,300
Total cash from sale at the end of 5 years (1)	$ 1,035,050	$ 1,081,900	$ 1,057,300

(1) Does not include the cash flow from the retained portion of the loan.

LOAN PORTFOLIO INFORMATION

Loan Portfolio Performance

Economic conditions have subjected many of our borrowers to financial stress. The operations of many of the limited service hospitality properties collateralizing our loans have been negatively impacted by the prolonged economic recession. We continue to experience a significant amount of payment delinquencies, slow pays, insufficient funds payments, late fees, non-payment or lack of timely payment of real estate taxes and franchise. fees, borrower requests for deferments of payment and liquidation and foreclosure activity.

For real estate secured loans, due to our borrowers' equity in their properties, the value of the underlying collateral, the cash flows from operations of the businesses and other factors such as having recourse to the guarantors, we have not historically experienced significant losses. However, if the economy or the commercial real estate market does not improve, we could experience an increase in credit losses. Additional changes to the facts and circumstances of the individual borrowers, the limited service hospitality industry and the economy may require the establishment of significant additional loan loss reserves and the effect on our results of operations and financial condition may be material.

Loan Activity

During the first half of 2010 we funded $22.7 million of SBA 7(a) Program loans. At June 30, 2010, December 31, 2009 and June 30, 2009, our outstanding commitments to fund loans were approximately $9.5 million, $20.7 million and $19.3 million, respectively. We expect that fundings during 2010 will be between $30 million and $40 million depending on our liquidity and the passage of legislation in Congress which would increase the 7(a) loan limit from $2 million to $5 million and extend the authorization to provide 90% guarantees on 7(a) loans and fee elimination for borrowers on 7(a) loans through December 31, 2010. These fundings will be predominantly through the SBA 7(a) Program.

In addition to our retained portfolio of $239.2 million at June 30, 2010, we service $47.6 million of aggregate principal balance of loans sold pursuant to Secondary Market Loan Sales. Prior to December 31, 2009, certain securitizations were not included in our retained portfolio but were included in our serviced portfolio. Effective January 1, 2010, due to a change in accounting rules, we now consolidate all of our securitizations. Since we retain a residual interest in the cash flows from these loans, the performance of these loans impacts our profitability and our cash available for dividend distributions. Therefore, we provide information on both our loans retained (the “Retained Portfolio”) and combined with sold loans that we service (the “Serviced Portfolio”).

Information on our Serviced Portfolio, including prepayment trends, was as follows:

	June 30,	December 31,				
	2010	2009	2008	2007	2006	2005
	(Dollars in thousands)					
Serviced Portfolio (1)	$ 286,789	$ 273,687	$ 275,530	$ 326,368	$ 397,567	$ 447,220
Loans funded (2)	$ 22,944	$ 30,435	$ 34,587	$ 33,756	$ 51,686	$ 49,942
Prepayments (2) (3)	$ 3,317	$ 12,795	$ 68,556	$ 84,137	$ 91,710	$ 41,049
% Prepayments (4)	2.4%	4.6%	21.0%	21.2%	20.5%	8.8%

(1) Serviced Portfolio outstanding at the period ended before loan loss reserves and deferred commitment fees.

(2) During the years ended December 31 and the six months ended June 30, 2010.

(3) Does not include balloon maturities of SBA 504 program loans.

(4) Represents prepayments as a percentage of the Serviced Portfolio outstanding as of the beginning of the applicable year. For the six months ended June 30, 2010, represents annualized prepayments as a percentage of our Serviced Portfolio outstanding.

Retained Portfolio Rollforward

Loans originated and principal repayments on our Retained Portfolio were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
	(In thousands)			
Loans Originated:				
Loans Funded:				
SBA 7(a) Program loans	$ 11,933	$ 4,266	$ 22,715	$ 7,802
Commercial mortgage loans	189	—	229	—
Total loans funded	12,122	4,266	22,944	7,802
Other Loan Transactions:				
2002 Joint Venture (1)	—	—	—	12,570
2000 Joint Venture (2)	—	—	22,912	—
1998 Partnership (2)	—	—	5,024	—
Loans originated to facilitate sales of real estate owned	1,050	—	3,325	—
Total loans originated	$ 13,172	$ 4,266	$ 54,205	$ 20,372
Principal Repayments and Other (3):				
Scheduled principal payments	$ 880	$ 1,612	$ 3,676	$ 3,441
Prepayments	841	4,100	3,058	4,100
Proceeds from sale of SBA 7(a) guaranteed loans (4)	2,007	6,894	2,007	7,677
Total principal repayments and other	$ 3,728	$ 12,606	$ 8,741	$ 15,218

(1) *We reached our "clean-up" call provision resulting in loans which were previously off-balance sheet being included in our Retained Portfolio.*

(2) *Due to a change in accounting rules effective January 1, 2010, the 2000 Joint Venture and the 1998 Partnership are now consolidated and included in our Retained Portfolio.*

(3) *Does not include principal reductions for loans transferred to real estate owned.*

(4) *For the three and six months ended June 30, 2010, represents reclassifications from secured borrowings — government guaranteed loans to loans receivable.*

Interest Rate and Yield Information

Interest rate and yield information on our Retained Portfolio were as follows:

	June 30, 2010	December 31, 2009	June 30, 2009
Weighted average contractual interest rate	5.7%	5.3%	6.0%
Annualized average yield (1)	6.0%	5.5%	5.9%

(1) *For the six month periods ended June 30, 2010 and 2009 and for the year ended December 31, 2009. In addition to interest income, the annualized average yield includes all fees earned and is adjusted by the provision for (reduction of) loan losses, net.*

The LIBOR and the prime rate used in determining interest rates to be charged to our borrowers during the third quarter of 2010 (set on July 1, 2010) is 0.53% and 3.25%, respectively, while the LIBOR and prime rate charged during the second quarter of 2010 (set on April 1, 2010) was 0.29% and 3.25%, respectively. To the extent LIBOR or the prime rate changes, we will have changes in interest income from our variable-rate loans.

Retained Portfolio Breakdown

Our Retained Portfolio was comprised of the following:

	June 30, 2010			December 31, 2009		
	Retained Portfolio		Weighted Average Interest	Retained Portfolio		Weighted Average Interest
	Amount	%	Rate	Amount	%	Rate
	(Dollars in thousands)					
Variable-rate — LIBOR	$ 131,610	55.3%	4.1%	$ 132,162	67.2%	4.0%
Fixed-rate	65,536	27.6%	9.0%	45,678	23.2%	9.0%
Variable-rate — prime	40,736	17.1%	5.6%	18,802	9.6%	5.4%
	$ 237,882	100.0%	5.7%	$ 196,642	100.0%	5.3%

Impaired Loans

Senior management closely monitors our impaired loans which are classified into two categories: Problem Loans and Special Mention Loans (together, “Impaired Loans”). Our Problem Loans are loans which are not complying with their contractual terms, the collection of the balance of the principal is considered unlikely and on which the fair value of the collateral is less than the remaining unamortized principal balance. Our Special Mention Loans are those loans that are either not complying or had previously not complied with their contractual terms but, in general, we expect a full recovery of the principal balance through either collection efforts or liquidation of collateral.

In addition to Impaired Loans, we have “watch list loans” as determined by management. Watch List loans are generally loans for which the borrowers are current on their payments; however, they may be delinquent on their property taxes, have requested a deferment, have franchise issues (non-payment of fees, loss of franchise and/or failure to meet franchise standards), insurance defaults or other contractual deficiencies.

At June 30, 2010 and December 31, 2009, we had loan loss reserves of $1,200,000 and $1,257,000, respectively, including general reserves of $850,000 and $650,000, respectively. Our provision for loan losses (excluding reductions of loan losses) as a percentage of our weighted average outstanding loans receivable was 0.13% and 0.14% during the six months ended June 30, 2010 and 2009, respectively. To the extent one or several of our loans experience significant operating difficulties and we are forced to liquidate the loans, future losses may be substantial.

Our loan categories were as follows on our retained loans receivable (balances represent our investment in the loans prior to loan loss reserves and deferred commitment fees):

	June 30, 2010		December 31, 2009		December 31, 2008	
	Amount	%	Amount	%	Amount	%
	(Dollars in thousands)					
Satisfactory	$ 221,349	92.5%	$ 177,129	89.3%	$ 156,303	86.6%
Watch List	15,487	6.5%	17,593	8.9%	12,507	6.9%
Special Mention	990	0.4%	759	0.4%	9,294	5.1%
Problem	1,347	0.6%	2,766	1.4%	2,501	1.4%
	$ 239,173	100.0%	$ 198,247	100.0%	$ 180,605	100.0%

Real Estate Owned and Foreclosure Activity

We begin foreclosure and liquidation proceedings when we determine the pursuit of these remedies is the most appropriate course of action. Foreclosure and bankruptcy are complex and sometimes lengthy processes that are subject to Federal and state laws and regulations.

We had foreclosure and sale activity during 2010. In January 2010, we sold an asset acquired through foreclosure for gross cash proceeds of $2,500,000 and recorded a gain of $76,000. In March 2010, we sold an asset acquired through foreclosure for $2,275,000 and financed the sale. During May 2010, we acquired an asset through deed in lieu of foreclosure, sold it for $1,125,000 and financed $1,050,000 of the sale price. No gains or losses were recorded on these transactions. During June 2010, we acquired a full service hospitality property through foreclosure. The estimated fair value of the property, as reduced for costs of selling, was estimated to be $1,250,000. We anticipate that we will operate this property until it can be sold.

We are currently in the process of foreclosure proceedings on several properties collateralizing our loans. Historically, subsequent to commencement of the foreclosure process, many borrowers brought their loans current; thus, we stopped the foreclosure process. Alternatively, borrowers have the option of seeking Federal bankruptcy protection which could delay the foreclosure process or modify the terms of the loan agreement. Typically, delays in the foreclosure process will have a negative impact on our results of operations and/or financial condition due to direct and indirect costs incurred and possible deterioration of the collateral. It is difficult to determine what impact the market disruptions will have on our borrowers whose collateral is in the process of foreclosure and the borrowers' ability to become current on their loans.

RESULTS OF OPERATIONS

Three Months Ended June 30, 2010 Compared to the Three Months Ended June 30, 2009

Overview

	Three Months Ended June 30,		Change	
	2010	2009	$	%
	(Dollars in thousands)			
Total revenues	$ 3,935	$ 3,872	$ 63	1.6%
Total expenses	$ 2,729	$ 2,396	$ 333	13.9%
Income from continuing operations	$ 1,226	$ 1,544	$ (318)	(20.6%)
Net income	$ 1,223	$ 1,564	$ (341)	(21.8%)

The comparability of our operations between 2010 and 2009 was impacted by the consolidation of previously off-balance sheet securitizations and the accounting change (effective January 1, 2010) for sale treatment on Secondary Market Loan Sales.

The consolidation of previously off-balance sheet entities caused a "gross-up" of our interest income and interest expense during 2010 as compared to separate one-line revenue recognition during 2009 as income from Retained Interests. In addition, the impact to our net income was impacted by a change in accounting rules related to Secondary Market Loan Sales that defers sale treatment on loans sold and records them as secured borrowings on a temporary basis (loans sold for premiums) for at least 90 days and eliminates sale treatment on loans sold and records them as secured borrowings on a permanent basis (loans sold for excess spread and loans sold for a cash premium and excess spread) for the life of the loan subsequent to December 31, 2009. However, for loans sold for a cash premium and excess spread, the cash premium will be amortized as a reduction to interest expense over the life of the loan. We recorded $167,000 in premium income during the three months ended June 30, 2010.

The primary causes of the reduction in net income from the second quarter of 2009 to the second quarter of 2010 were:

- A reduction in base LIBOR from 1.21% during the second quarter of 2009 to 0.29% during the second quarter of 2010. The impact to net income was approximately $225,000; and
- An increase in expenses related to loans in the process of foreclosure of $117,000. We did not have any loans in the process of foreclosure during the second quarter of 2009.

More detailed comparative information on the composition of and changes in our revenues and expenses is provided below.

Revenues

The increase in interest income of $713,000 was primarily attributable to the consolidation of our previously off-balance sheet securitizations partially offset by a decrease in LIBOR. Interest income attributable to these securitizations totaled approximately $860,000 during the three months ended June 30, 2010. At June 30, 2010, approximately 72% of our loans had variable interest rates. The base LIBOR charged to our borrowers decreased from 1.21% during the three months ended June 30, 2009 to 0.29% during the three months ended June 30, 2010. On our average LIBOR based portfolio outstanding of $132.4 million during the second quarter of 2010, the 92 basis point drop in LIBOR decreased interest income by approximately $300,000.

Income from Retained Interests decreased $747,000 due to a change in accounting rules which required that our off-balance sheet securitizations be consolidated effective January 1, 2010. As a result, our income from Retained Interests decreased to $34,000 during the three months ended June 30, 2010. We expect that income from Retained Interests will remain at its current level during the second half of 2010.

Other income consisted of the following:

	Three Months Ended June 30,	
	2010	2009
	(In thousands)	
Premium income	$ 167	$ 59
Prepayment fees	93	46
Servicing income	86	103
Loan related income — other	38	60
Other	19	38
	$ 403	$ 306

Premium income results from the recognition of the sale of the government guaranteed portion of SBA 7(a) Program loans into the secondary market. Beginning January 1, 2010, due to a change in accounting rules, any premium income to be recognized is deferred for at least 90 days until any potential contingency period for having to refund the premiums has been satisfied. We anticipate that we will record approximately $510,000 in premium income during the third quarter of 2010.

Interest Expense

Interest expense consisted of the following:

	Three Months Ended June 30,	
	2010	2009
	(In thousands)	
Structured notes payable	$ 335	$ 88
Junior subordinated notes	245	309
Revolver	198	173
Debentures payable	124	123
Other	109	97
	$ 1,011	$ 790

The weighted average cost of our funds was 4.1% during both the quarters ended June 30, 2010 and 2009. Interest expense on the junior subordinated notes decreased as a result of decreases in LIBOR.

The increase in interest expense on structured notes payable is due to the consolidation of the off-balance sheet securitizations. Beginning in September 2009, we consolidated the 2003 Joint Venture including its structured notes and their related interest expense. At June 30, 2010, the 2003 Joint Venture notes bear interest at LIBOR plus 2.5%. Effective January 1, 2010, due to a change in accounting rules, we now consolidate the structured notes of the 2000 Joint Venture and the 1998 Partnership and their related interest expense. At June 30, 2010, the 2000 Joint Venture notes bear interest at a fixed rate of 7.28% while the 1998 Partnership notes bear interest at the prime rate less 1%.

In addition to the consolidation of the structured notes payable above, effective January 1, 2010, we now record secured borrowings relating to sales of the guaranteed portion of our SBA 7(a) loans either temporarily or permanently depending on how the loan is sold.

During March 2010, we redeemed 20,000 shares of $100 par value, 4% cumulative preferred stock of one of our SBICs held by the SBA due in May 2010. No gain or loss was recorded on the redemption.

Other Expenses

General and administrative expense increased $110,000 during the three months ended June 30, 2010 compared to the three months ended June 30, 2009. General and administrative expenses are comprised of (1) corporate overhead including legal and professional expenses, sales and marketing expenses, public company and regulatory costs and (2) expenses related to assets currently in the process of foreclosure. Our corporate overhead remained consistent at $527,000 during the three months ended June 30, 2010 compared to $534,000 during the three months ended June 30, 2009. Expenses related to assets currently in the process of foreclosure totaled $117,000 during the three months ended June 30, 2010 primarily related to a full service hospitality property. We foreclosed on the full service hospitality property during June 2010. The expenses incurred during the foreclosure process for problem loans are primarily related to property taxes incurred, legal fees, protection of the asset and operating deficits funded to court-appointed receivers. We expect to continue to incur general and administrative expenses related to problem loans until the foreclosure processes are completed; however, we are unable to estimate these expenses and these expenses may be material. Once the foreclosure processes are completed, we expect that we will incur net losses which will be included in discontinued operations related to these properties. We did not have any assets in the process of foreclosure during the three months ended June 30, 2009.

Six Months Ended June 30, 2010 Compared to the Six Months Ended June 30, 2009

Overview

	Six Months Ended June 30,		Change	
	2010	2009	$	%
	(Dollars in thousands)			
Total revenues	$ 7,390	$ 7,863	$ (473)	(6.0%)
Total expenses	$ 5,025	$ 4,773	$ 252	5.3%
Income from continuing operations	$ 2,493	$ 3,140	$ (647)	(20.6%)
Net income	$ 2,501	$ 3,190	$ (689)	(21.6%)

The comparability of our operations between 2010 and 2009 was impacted by the consolidation of previously off-balance sheet securitizations and the accounting change (effective January 1, 2010) for sale treatment on Secondary Market Loan Sales.

The consolidation of these previously off-balance sheet entities caused a “gross-up” of our interest income and interest expense during 2010 as compared to separate one-line revenue recognition during 2009 as income from Retained Interests. In addition, the impact to our net income was impacted by a change in accounting rules related to Secondary Market Loan Sales that defers sale treatment on loans sold and records them as secured borrowings on a temporary basis (loans sold for premiums) for at least 90 days and eliminates sale treatment on loans sold and records them as secured borrowings on a permanent basis (loans sold for excess spread and loans sold for a cash premium and excess spread) for the life of the loan subsequent to December 31, 2009. However, for loans sold for a cash premium and excess spread, the premium will be amortized as a reduction to interest expense over the life of the loan. We recorded $167,000 in premium income during the six months ended June 30, 2010.

The primary causes of the reduction in net income from 2009 to 2010 were:

- A reduction in average base LIBOR from 1.32% during the six months ended June 30, 2009 to 0.27% during the six months ended June 30, 2010. The impact to net income was approximately $500,000;
- Included in income from Retained Interests was approximately $320,000 of income, primarily unanticipated prepayment fees, during the six months ended June 30, 2009 while there was no comparable revenue during the six months ended June 30, 2010; and
- An increase in expenses related to loans in the process of foreclosure of $305,000. We did not have any loans in the process of foreclosure during the six months ended June 30, 2009; partially offset by
- A decrease in provision for (reduction of) loan losses of $301,000 due primarily to positive changes in (1) the financial condition of certain borrowers and (2) collateral valuation on a limited service hospitality loan.

More detailed comparative information on the composition of and changes in our revenues and expenses is provided below.

Revenues

The increase in interest income of $1,079,000 was primarily attributable to the consolidation of our previously off-balance sheet securitizations partially offset by a decrease in LIBOR. Interest income attributable to these securitizations totaled approximately $1,585,000 during the six months ended June 30, 2010. At June 30, 2010, approximately 72% of our loans had variable interest rates. The average base LIBOR charged to our borrowers decreased from 1.32% during the six months ended June 30, 2009 to 0.27% during the six months ended June 30, 2010. On our average LIBOR based portfolio outstanding of $132.3 million during the first half of 2010, the 105 basis point drop in LIBOR decreased interest income by approximately $700,000.

Income from Retained Interests decreased $1,622,000 due to a change in accounting rules which required that our off-balance sheet securitizations be consolidated effective January 1, 2010. As a result, our income from Retained Interests decreased to $75,000 during the six months ended June 30, 2010. We expect that income from Retained Interests will remain at its current level during the second half of 2010.

Other income consisted of the following:

	Six Months Ended June 30,	
	2010	2009
	(In thousands)	
Premium income	$ 167	$ 68
Servicing income	164	198
Prepayment fees	135	46
Loan related income — other	96	129
Other	38	89
	$ 600	$ 530

Premium income results from the sale of the government guaranteed portion of SBA 7(a) Program loans into the secondary market. Beginning January 1, 2010, due to a change in accounting rules, any premium income to be recognized is deferred for at least 90 days until any potential contingency period for having to refund the premiums has been satisfied. We anticipate that we will record approximately $510,000 in premium income during the third quarter of 2010.

Interest Expense

Interest expense consisted of the following:

	Six Months Ended June 30,	
	2010	2009
	(In thousands)	
Structured notes payable	$ 681	$ 184
Junior subordinated notes	484	628
Revolver	398	355
Debentures payable	247	246
Other	190	183
	$ 2,000	$ 1,596

The weighted average cost of our funds for the six months ended June 30, 2010 was 3.9% compared to 4.1% during the six months ended June 30, 2009. Interest expense on the junior subordinated notes decreased as a result of decreases in LIBOR.

The increase in interest expense on structured notes payable is due to the consolidation of the off-balance sheet securitizations. Beginning in September 2009, we consolidated the 2003 Joint Venture including its structured notes and their related interest expense. At June 30, 2010, the 2003 Joint Venture notes bear interest at LIBOR plus 2.5%. Effective January 1, 2010, due to a change in accounting rules, we now consolidate the structured notes of the 2000 Joint Venture and the 1998 Partnership and their related interest expense. At June 30, 2010, the 2000 Joint Venture notes bear interest at a fixed rate of 7.28% while the 1998 Partnership notes bear interest at the prime rate less 1%.

In addition to the consolidation of the structured notes payable above, effective January 1, 2010, we now record secured borrowings relating to sales of the guaranteed portion of our SBA 7(a) loans either temporarily or permanently depending on how the loan is sold.

During March 2010, we redeemed 20,000 shares of $100 par value, 4% cumulative preferred stock of one of our SBICs held by the SBA due in May 2010. No gain or loss was recorded on the redemption.

Other Expenses

General and administrative expense increased $235,000 during the six months ended June 30, 2010 compared to the six months ended June 30, 2009. General and administrative expenses are comprised of (1) corporate overhead including legal and professional expenses, sales and marketing expenses, public company and regulatory costs and (2) expenses related to assets currently in the process of foreclosure. Our corporate overhead decreased to $907,000 during the six months ended June 30, 2010 compared to $977,000 during the six months ended June 30, 2009 primarily related to a decrease in legal fees related to strategic initiatives. Expenses related to assets currently in the process of foreclosure totaled $305,000 during the six months ended June 30, 2010 primarily related to a full service hospitality property. We foreclosed on the full service hospitality property during June 2010. The expenses incurred during the foreclosure process for problem loans are primarily related to property taxes incurred, legal fees, protection of the asset and operating deficits funded to court-appointed receivers. We expect to continue to incur general and administrative expenses related to problem loans until the foreclosure processes are completed; however, we are unable to estimate these expenses and these expenses may be material. Once the foreclosure processes are completed, we expect that we will incur net losses which will be included in discontinued operations related to these properties. We did not have any assets in the process of foreclosure during the six months ended June 30, 2009.

Provision for (reduction of) loan losses, net, was a reduction of $98,000 during the six months ended June 30, 2010 compared to a provision of $203,000 during the six months ended June 30, 2009. The reduction of loan losses during the six months ended June 30, 2010 was primarily related to positive changes in (1) the financial condition of certain borrowers and (2) collateral valuation on a limited service hospitality loan.

Income tax benefit was $128,000 during the six months ended June 30, 2010 compared to $50,000 during the six months ended June 30, 2009. A deferred tax benefit of approximately $565,000 was recorded by one of our taxable REIT subsidiaries as a result of a book loss while current income tax expense of the subsidiary was approximately $350,000. The reason for the difference is the new accounting rules that defer gain recognition treatment on Secondary Market Loan Sales. During the six months ended June 30, 2010, significant gains of approximately $1,858,000 were deferred for book purposes and recorded as gains for income tax purposes.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flow Analysis

Information on our cash flow was as follows:

	Six Months Ended June 30,		
	2010	2009	Change
		(In thousands)	
Cash provided by (used in) operating activities	$ (15,773)	$ 2,163	$ (17,936)
Cash provided by investing activities	$ 7,555	$ 4,707	$ 2,848
Cash provided by (used in) financing activities	$ 6,789	$ (8,531)	$ 15,320

Due to a change in accounting rules effective January 1, 2010 which delays or eliminates sale treatment related to our Secondary Market Loan Sales, cash used to originate loans held for sale are a use of funds from operating activities while proceeds from the sale of guaranteed loans are now included in financing activities.

Operating Activities

We used cash in operating activities of $15,773,000 during the six months ended June 30, 2010. Operating income was typically used to fund our dividends. Since operating cash flows also includes lending activities, it is necessary to adjust our cash flow from operating activities for our lending activities to determine coverage of our dividends from operations. Therefore, we adjust net cash provided by operating activities to “Modified Cash.” Management believes that our modified cash available for dividend distributions (“Modified Cash”) is a more appropriate indicator of operating cash coverage of our dividend payments than cash flow provided by (used in) operating activities. Modified Cash is calculated by adjusting our cash provided by (used in) operating activities by (1) the change in operating assets and liabilities and (2) loans funded, held for sale, net of proceeds from sale of guaranteed loans and principal collected on loans (“Operating Loan Activity”). Modified Cash is one of the measurements used by our Board of Trust Managers (the “Board”) in its determination of dividends and their timing. In respect to our dividend policy, we believe that the disclosure of Modified Cash adds additional transparency to our dividend calculation and intentions. However, Modified Cash may differ significantly from dividends paid due to timing differences between book income and taxable income and timing of payment of dividends to eliminate or reduce Federal income taxes or excise taxes at the REIT level.

The following reconciles net cash provided by (used in) operating activities to Modified Cash:

	Six Months Ended June 30,	
	2010	2009
	(In thousands)	
Net cash provided by (used in) operating activities	$ (15,773)	$ 2,163
Change in operating assets and liabilities	(1,166)	2,318
Operating Loan Activity	19,826	(1,223)
Modified Cash	$ 2,887	$ 3,258

To the extent Modified Cash does not cover the current dividend distribution rate or if additional cash is needed based on our working capital needs, the Board may choose to modify its current dividend policy. During the six months ended June 30, 2010 and 2009, dividend distributions were greater than our Modified Cash by $510,000 and $3,037,000, respectively. To the extent we need working capital to fund any shortfall in operating cash flows to cover our dividend distribution, we would need to borrow the funds from our Revolver or use funds from the repayment of principal on loans receivable.

Investing Activities

During the six months ended June 30, 2010 and 2009, the primary source of funds was principal collected on loans, net of loans funded of $5,559,000 and $6,193,000, respectively. We expect that this will continue to be our primary source of funds from investing activities during the remainder of 2010. In addition, during the six months ended June 30, 2010, we sold assets included in real estate owned and collected net cash proceeds of $2,291,000.

Financing Activities

We used funds from financing activities during the six months ended June 30, 2010 and 2009 primarily to pay dividends of $3,397,000 and $6,295,000, respectively, and for the repurchase of common shares during the six months ended June 30, 2009. During the six months ended June 30, 2010, we also used $4.1 million in funds from financing activities for repayment on our Revolver. Due to a change in accounting rules effective January 1, 2010, proceeds from Secondary Market Loan Sales are now included within financing activities compared to operating activities prior to January 1, 2010. Proceeds from these Secondary Market Loans Sales during the six months ended June 30, 2010 were $18,639,000. In addition, during the six months ended June 30, 2010, we redeemed $2,000,000 of redeemable preferred stock of subsidiary due in May 2010 using cash on hand of one of our SBIC subsidiaries.

Sources and Uses of Funds

Liquidity Summary

Liquidity is a measure of our ability to meet potential cash requirements, including ongoing commitments to fund loans and other investments, pay dividends, fund debt service and for other general corporate purposes. Our primary sources of funds to meet our short-term liquidity needs consist of (1) Secondary Market Loan Sales, (2) proceeds from principal and interest payments, including prepayments, and (3) borrowings under any available short-term credit facilities. We believe these sources of funds will be sufficient to meet our liquidity requirements in the short-term. To a lesser extent, and to the extent available to us, we may utilize (1) proceeds from potential loan and asset sales, (2) new financings or securitization offerings and (3) proceeds from potential common or preferred equity offerings.

Our Revolver matures on December 31, 2010. The amount available under the Revolver is currently $30 million and reduces to $25 million on October 1, 2010. Upon maturity the amount available will be $20 million. We are currently addressing the extension of our facility for an additional year with our lender.

Our net capital outlay for loans during the second half of 2010 (loans to be funded less proceeds from loans to be sold) is anticipated to be approximately $4.0 million. Our anticipated scheduled principal payments on our loan portfolio during the second half of 2010 are $3.0 million which would be available to repay a portion of the existing balance under the Revolver. Based on the above cash activity and other factors, we currently anticipate that the balance outstanding under our Revolver will be approximately $20.0 million, without any proceeds from loan principal prepayments or cash sales of real estate owned or alternatively, any unforeseen uses of funds.

For 2011, we will need funds to originate loans. To the extent the maximum guarantees under the SBA 7(a) Program are capped at 75%, we anticipate that we would need between $7.5 million and $10.0 million in 2011 to fund our SBA 7(a) anticipated gross fundings of between $30.0 million and $40.0 million. Our anticipated scheduled principal payments on our loan portfolio in 2011 are $6.0 million which would be available to repay a portion of any balance under the Revolver. Accordingly, without any loan principal prepayments, we would need additional borrowing capacity of between $1.5 million and $4.0 million. This analysis does not take into account potential additional working capital needs such as (1) timing differences between when we originate a loan and when we receive the proceeds from the sold loan, (2) continuation of a cash dividend that exceeds our cash generated from operations, (3) outlay of funds needed to protect our loans receivable during the foreclosure process or (4) unforeseen cash needs.

We believe that we will be able to get the liquidity to fund our loans in 2011 by extending and increasing our Revolver to between $25.0 million and $30.0 million and through funds provided by principal prepayments on our loans. To the extent we are unable to extend or increase our Revolver, we may have to reduce the level of loan originations in 2011.

Due to current market conditions, we cannot access debt capital through new or increased warehouse lines, new securitization issuances or new trust preferred issuances. We continue to explore ways to extend or refinance our short-term Revolver; however, in the event we are not able to extend or refinance our Revolver or successfully secure alternative financing, we will rely on Modified Cash, principal payments (including prepayments), and (if necessary) proceeds from asset and loan sales to satisfy our liquidity requirements.

If we are unable to make required payments under our borrowings, breach any representation or warranty of our borrowings or violate any covenant, our lenders may accelerate the maturity of our debt or require us to liquidate pledged collateral or force us to take other actions. In connection with an event of default under our Revolver, the lender is permitted to accelerate repayment of all amounts due, terminate commitments thereunder, and liquidate the mortgage loan collateral held as security for the Revolver to satisfy any balance outstanding and due pursuant to the Revolver. Any such event may have a material adverse effect on our liquidity, the value of our common shares and the ability to pay dividends to our shareholders.

Sources of Funds

In general, we require liquidity to originate new loans and repay principal on our debt. Our operating revenues are typically utilized to pay our operating expenses, interest and dividends. We have been utilizing principal collections on loans receivable and borrowings under our Revolver as our primary sources of funds. In addition, historically we utilized a combination of the following sources to generate funds:

- Structured loan financings or sales;
- Issuance of SBA debentures;
- Secondary Market Loan Sales;
- Issuance of junior subordinated notes; and/or
- Common equity issuance.

As discussed previously, these markets (with the exception of SBA debentures and Secondary Market Loan Sales) are not available to us at the present time and there can be no assurance that they will be available in the future. At our current share price, we do not intend to issue common shares. Since 2004, our working capital has primarily been provided through credit facilities, the issuance of junior subordinated notes and principal payments (including prepayments) on loans receivable. Prior to 2004, our primary source of long-term funds was structured loan sale transactions. At the current time, there is a limited market for commercial loan asset-backed securitizations. We cannot anticipate when, or if, this market will be available to us in the future. Until this market becomes more readily available, our ability to grow is limited.

The limited amount of capital available to originate new loans has caused us to restrict non-SBA 7(a) Program loan origination activity. Depending on the availability of other sources of capital including principal prepayments on our loans, we may have to curtail some SBA 7(a) lending opportunities in 2010. A reduction in the availability of the above sources of funds could have a material adverse effect on our financial condition and results of operations. If these sources are not available in the future, we may have to originate loans at further reduced levels or sell assets, potentially on unfavorable terms.

Our Revolver matures December 31, 2010. We are currently addressing the extension of our facility for an additional year with our lender. There can be no assurance that we will be able to extend or refinance our Revolver. As a result, our ability to grow will be further limited unless we are subsequently able to increase the aggregate availability under any extension or replacement of the Revolver or secure additional financing. To the extent we need additional capital for unanticipated items, there can be no assurance that we would be able to increase the amount available under any short-term credit facilities or identify other sources of funds at an acceptable cost, if at all.

We rely on Secondary Market Loan Sales to create availability and/or repay principal due on our Revolver. Once fully funded, we typically sell the government guaranteed portion of our SBA 7(a) Program loans. The market demand for Secondary Market Loan Sales may decline or be temporarily suspended. To the extent we are unable to execute Secondary Market Loan Sales in the normal course of business, our financial condition and results of operations could be adversely affected.

We have a debt-to-equity ratio of 0.7:1 at June 30, 2010. This ratio is below that of typical specialty commercial finance companies.

As a REIT, we must distribute to our shareholders at least 90% of our REIT taxable income to maintain our tax status under the Code. Accordingly, to the extent the sources above represent taxable income, such amounts have historically been distributed to our shareholders. In general, should we receive less cash from our portfolio of investments, we can lower the dividend so as not to cause any material cash shortfall. During 2010, we anticipate that our Modified Cash will be utilized to fund our expected 2010 dividend distributions and generally will not be available to fund portfolio growth or for the repayment of principal due on our debt.

The Revolver requires us to meet certain covenants, the most restrictive of which provides for a maximum amount of problem assets as defined in the agreement. The maximum problem assets cannot exceed 10% of beneficiaries’ equity calculated on a quarterly basis. In addition, we have (1) an asset coverage test based on our cash and cash equivalents and loans receivable as a ratio to our senior debt of 1.25 times, (2) a covenant that limits our ability to pay out returns of capital as part of our dividends and (3) a minimum equity requirement of $145 million. At June 30, 2010, we were in compliance with the covenants of this facility. While we anticipate maintaining compliance with these covenants, there can be no assurance that we will be able to do so.

We anticipate requesting a commitment from the SBA for $10 million of debentures during the third quarter of 2010 which we expect to be approved during the fourth quarter of 2010. These debentures would be used to fund loans within our SBICs to the extent necessary.

Uses of Funds

Currently, the primary use of our funds is to originate loans and for repayment of principal on our debt. Our outstanding commitments to fund new loans were $9.5 million at June 30, 2010, the majority of which were for prime-rate based loans to be originated by First Western, the government guaranteed portion of which is intended to be sold pursuant to Secondary Market Loan Sales. Our net working capital outlay would be approximately $4.3 million related to these loans; however, the First Western loans cannot be sold until they are fully funded. Commitments have fixed expiration dates. Since some commitments expire without the proposed loan closing, total committed amounts do not necessarily represent future cash requirements. During 2010, we anticipate loan fundings will range from $30 million to $40 million. In addition, we use funds for operating deficits and holding costs of our real estate owned and properties in the process of foreclosure.

There may be several months between when the initial balance of an SBA 7(a) Program loan is funded and it is fully funded and can be sold. In these instances, our liquidity would be affected in the short-term. In addition, once fully funded, we anticipate the ability to sell the government guaranteed portion of our SBA 7(a) Program loans into the secondary market.

The amount available under the Revolver is currently $30 million and will be reduced to $25 million on October 1, 2010. The amount available under the Revolver will further reduce to $20 million on December 31, 2010 at which time the Revolver will also mature.

We may repurchase loans from the securitizations which have become “charged-off” as defined in the transaction documents either through delinquency or initiation of foreclosure. We may be required to use restricted cash of our securitizations to repay a loan within a securitization to the structured noteholders if it is deemed “charged-off” per the transaction documents. If we choose to repurchase a loan from a securitization using our Revolver, the balance due on our structured notes payable would decrease and the balance due under our short-term Revolver would increase.

We anticipate prepayment (without any prepayment penalty) during the third quarter of 2010 of the mortgage note of our unconsolidated subsidiary of approximately $1.0 million which matures in January 2011 using our Revolver.

We may pay dividends in excess of our funds from operating activities to maintain our REIT status or as approved by our Board of Trust Managers. During the six months ended June 30, 2010, our sources of funds for our dividend distributions of approximately $3.4 million were Modified Cash of approximately $2.9 million and principal collections on our loans receivable of approximately $0.5 million.

SUMMARIZED CONTRACTUAL OBLIGATIONS, COMMITMENTS AND CONTINGENCIES

The following summarizes our contractual obligations at June 30, 2010:

Contractual Obligations (1)	Payments Due by Period				
	Total	Less than 1 year	1 to 3 years	3 to 5 years	More than 5 years
	(In thousands, except footnotes)				
Debt:					
Debentures payable (2)	$ 8,190	$ —	$ —	$ 4,190	$ 4,000
Structured notes payable (3)	25,272	3,620	8,086	8,336	5,230
Secured borrowings — government guaranteed loans (3)	17,628	6,148	690	728	10,062
Revolver	18,900	18,900	—	—	—
Junior subordinated debt (4)	27,070	—	—	—	27,070
Interest:					
Consolidated debt (5)	34,931	3,679	5,359	4,099	21,794
Mortgage note of unconsolidated subsidiary	51	51	—	—	—
Other Contractual Obligations:					
Mortgage note of unconsolidated subsidiary (6)	1,048	1,048	—	—	—
Severance and related benefits	148	20	128	—	—
Operating lease (7)	295	220	75	—	—
Total contractual cash obligations	$ 133,533	$ 33,686	$ 14,338	$ 17,353	$ 68,156

(1) Does not include $3.0 million of cumulative preferred stock of subsidiary (valued at $900,000 on our consolidated balance sheet) and related dividends (recorded as interest expense) of $90,000 annually which has no maturity date.

(2) Debentures payable are presented at face value.

(3) Principal payments are dependent upon cash flows received from the underlying loans. Our estimate of their repayment is based on scheduled principal payments on the underlying loans. Our estimate will differ from actual amounts to the extent we experience prepayments and/or losses. In addition, secured borrowings — loans sold for premiums are treated as current due to the contingency period expiring in approximately 90 days.

(4) The junior subordinated notes may be redeemed at our option, without penalty and are subordinated to PMC Commercial's existing debt.

(5) Calculated using the variable rate in effect at June 30, 2010. In addition, for our Revolver, assumes current balance outstanding through maturity date.

(6) Represents a mortgage note with a fixed interest rate of 8.5% of an unconsolidated subsidiary due January 1, 2011.

(7) Represents future minimum lease payments under our operating lease for office space.

Our commitments at June 30, 2010 are summarized as follows:

Commitments	Total Amounts Committed	Amount of Commitment Expiration Per Period			
		Less than 1 year	1 to 3 years	3 to 5 years	After 5 years
		(In thousands)			
Loan commitments	$ 9,549	$ 9,549	$ —	$ —	$ —

See Note 13 to the Consolidated Financial Statements for a detailed discussion of commitments and contingencies.

DIVIDENDS

Our shareholders are entitled to receive dividends when and as declared by the Board. In determining dividend policy, the Board considers many factors including, but not limited to, expectations for future earnings, REIT taxable income and maintenance of REIT status, the economic environment, our ability to obtain leverage, our loan portfolio performance and actual and anticipated Modified Cash. In order to maintain REIT status, PMC Commercial is required to pay out 90% of REIT taxable income. Consequently, the dividend rate on a quarterly basis will not necessarily correlate directly to any individual factor.

In order to meet our 2009 taxable income distribution requirements, we made an election under the Code to treat a portion of the distributions declared in 2010 as distributions of 2009's REIT taxable income. These distributions are known as spillover dividends. The Board anticipates utilizing the shortfall caused by spillover dividends to allow dividends declared in 2010 to exceed our 2010 REIT taxable income.

We have certain covenants within our debt facilities that limit our ability to pay out returns of capital as part of our dividends. These restrictions have not historically limited the amount of dividends we have paid and management does not believe that they will restrict future dividend payments.

REIT TAXABLE INCOME

REIT taxable income is a financial measure that is presented quarterly to assist investors in analyzing our performance and is one of the factors utilized by our Board in determining the level of dividends to be paid to our shareholders.

The following reconciles net income to REIT taxable income (loss):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
	(In thousands)			
Net income	$ 1,223	$ 1,564	$ 2,501	$ 3,190
Book/tax difference on depreciation	(14)	(14)	(26)	(28)
Book/tax difference on gains related to real estate	(2)	(20)	387	(50)
Book/tax difference on Retained Interests, net	—	(238)	—	(411)
Severance payments	(8)	(1,407)	(14)	(1,429)
Book/tax difference on amortization and accretion	(25)	(31)	(51)	(63)
Loan valuation	(361)	62	(558)	154
Other book/tax differences, net	(78)	(74)	(114)	(58)
Subtotal	735	(158)	2,125	1,305
Less: TRS net loss, net of tax	60	154	293	140
REIT taxable income (loss)	$ 795	$ (4)	$ 2,418	$ 1,445
Distributions declared	$ 1,689	$ 1,687	$ 3,377	$ 4,069
Weighted average common shares outstanding	10,550	10,548	10,549	10,599

As a REIT, PMC Commercial generally will not be subject to corporate level Federal income tax on net income that is currently distributed to shareholders provided the distribution exceeds 90% of REIT taxable income. We may make an election under the Code to treat a portion of distributions declared in the current year as distributions of the prior year's taxable income. Upon election, the Code provides that, in certain circumstances, a dividend declared subsequent to the close of an entity's taxable year and prior to the extended due date of the entity's tax return may be considered as having been made in the prior tax year in satisfaction of income distribution requirements.

ITEM 3.
Quantitative and Qualitative Disclosures About Market Risk

Market risk is the exposure to loss resulting from changes in various market metrics. We are subject to market risk including liquidity risk, real estate risk and interest rate risk as described below. Although management believes that the quantitative analysis on interest rate risk below is indicative of our sensitivity to interest rate changes, it does not adjust for potential changes in credit quality, size and composition of our balance sheet and other business developments that could affect our financial position and net income. Accordingly, no assurances can be given that actual results would not differ materially from the potential outcome simulated by these estimates.

Liquidity Risk

Liquidity risk is the potential that we would be unable to meet our obligations as they come due because of an inability to liquidate assets or obtain funding. We are subject to changes in the debt and collateralized mortgage markets. These markets are currently experiencing disruptions, which could have an adverse impact on our earnings and financial condition.

Current conditions in the debt markets include lack of liquidity and large risk adjusted premiums. These conditions have increased the cost and reduced the availability of financing sources. The market for trading in asset-backed securities continues to experience disruptions resulting from reduced investor demand for these securities and increased investor yield requirements. In light of these market conditions, we expect to finance our loan portfolio in the short-term with our current capital and any available short-term credit facilities.

Real Estate Risk

The value of our commercial mortgage loans and our ability to sell such loans, if necessary, are impacted by market conditions that affect the properties that are the primary collateral for our loans. Property values and operating income from the properties may be affected adversely by a number of factors, including, but not limited to:

- national, regional and local economic conditions;
- significant rises in gasoline prices within a short period of time if there is a concurrent decrease in business and leisure travel;
- local real estate conditions (including an oversupply of commercial real estate);
- natural disasters including hurricanes and earthquakes, acts of war and/or terrorism and other events that may cause performance declines and/or losses to the owners and operators of the real estate securing our loans;
- changes or continued weakness in the underlying value of limited service hospitality properties;
- construction quality, construction cost, age and design;
- demographic factors;
- increases in operating expenses (such as energy costs) for the owners of the properties; and
- limitations in the availability and cost of leverage.

In the event property cash flows decrease, a borrower may have difficulty repaying our loan, which could result in losses to us. In addition, decreases in property values reduce the value of the collateral and the potential proceeds available to borrowers to repay our loans, which could also cause us to suffer losses. Decreases in property values could reduce the value of our real estate owned which could cause us to suffer losses.

The following analysis of our provision for loan losses quantifies the negative impact to our net income from increased losses on our Retained Portfolio:

Provision for loan losses	Six Months Ended June 30, 2010	Year Ended December 31, 2009	Six Months Ended June 30, 2009
		(In thousands)	
As reported (1)	$ 306	$ 1,076	$ 267
Annual loan losses increase by 50 basis points (2)	884	2,027	738
Annual loan losses increase by 100 basis points (2)	1,462	2,977	1,209

(1) Excludes reductions of loan losses

(2) Represents provision for loan losses based on increases in losses as a percentage of our weighted average loans receivable for the periods indicated.

Interest Rate Risk

Interest rates are highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors.

Since our loans are predominantly variable-rate, based on LIBOR or the prime rate, our operating results will depend in large part on LIBOR or the prime rate. One of the primary determinants of our operating results is differences between the income from our loans and our borrowing costs. As a result, most of our borrowings are also based on LIBOR or the prime rate. The objective of this strategy is to minimize the impact of interest rate changes on our net interest income.

VALUATION OF LOANS

Our loans are recorded at cost and adjusted by net loan origination fees and discounts (which are recognized as adjustments of yield over the life of the loan) and loan loss reserves. In order to determine the estimated fair value of our loans, we use a present value technique for the anticipated future cash flows using certain assumptions including a current market discount rate, potential prepayment risks and loan losses. If we were required to sell our loans at a time we would not otherwise do so, there can be no assurance that management's estimates of fair values would be obtained and losses could be incurred.

At June 30, 2010, our loans are approximately 72% variable-rate at spreads over LIBOR or the prime rate. Increases or decreases in interest rates will generally not have a material impact on the fair value of our variable-rate loans. We had $172.4 million of variable-rate loans at June 30, 2010. The estimated fair value of our variable-rate loans (approximately $166.0 million at June 30, 2010) is dependent upon several factors including changes in interest rates and the market for the type of loans we have originated.

We had $65.5 million and $45.7 million of fixed-rate loans at June 30, 2010 and December 31, 2009, respectively. The estimated fair value of these fixed-rate loans approximates their cost and is dependent upon several factors including changes in interest rates and the market for the types of loans that we have originated. Since changes in market interest rates do not affect the interest rates on our fixed-rate loans, any changes in these rates do not have an immediate impact on our interest income. Our interest rate risk on our fixed-rate loans is primarily related to loan prepayments and maturities.

The average maturity of our loan portfolio is less than its average contractual terms because of prepayments. Assuming market liquidity, the average life of mortgage loans tends to increase when the current mortgage rates are substantially higher than rates on existing mortgage loans and, conversely, decrease when the current mortgage rates are substantially lower than rates on existing mortgage loans (due to refinancing of fixed-rate loans).

INTEREST RATE SENSITIVITY

At June 30, 2010 and December 31, 2009, we had $172.4 million and $151.0 million of variable-rate loans, respectively, and $74.8 million and $58.4 million of variable-rate debt, respectively. On the difference between our variable-rate loans and our variable-rate debt ($97.6 million and $92.6 million at June 30, 2010 and December 31, 2009, respectively) we have interest rate risk. To the extent variable rates decrease, our interest income net of interest expense would decrease.

The sensitivity of our variable-rate loans and debt to changes in interest rates is regularly monitored and analyzed by measuring the characteristics of our assets and liabilities. We assess interest rate risk in terms of the potential effect on interest income net of interest expense in an effort to ensure that we are insulated from any significant adverse effects from changes in interest rates. As a result of our predominately variable-rate portfolio, our earnings are susceptible to being reduced during periods of lower interest rates. Based on a sensitivity analysis of interest income and interest expense at June 30, 2010 and December 31, 2009, if the consolidated balance sheet were to remain constant and no actions were taken to alter the existing interest rate sensitivity, each hypothetical 100 basis point reduction in interest rates would reduce net income by approximately $976,000 and $926,000, respectively, on an annual basis. Since LIBOR has already been reduced to historically low levels, further significant negative impacts from lower LIBOR interest rates is not anticipated. In addition, as a REIT, the use of hedging interest rate risk is typically only provided on debt instruments due to potential negative REIT compliance to the extent the hedging strategy was based on our investments. Benefits derived from hedging strategies not based on debt instruments (*i.e.*, investments) may be deemed bad income for REIT qualification purposes. The use of a hedge strategy (on our debt instruments) would only be beneficial to fix our cost of funds and hedge against rising interest rates.

DEBT

Our debt is comprised of SBA debentures, junior subordinated notes, the Revolver, structured notes and secured borrowings — government guaranteed loans. At June 30, 2010 and December 31, 2009, approximately $22.2 million and $10.1 million, respectively, of our debt had fixed rates of interest and was therefore not affected by changes in interest rates. Our variable-rate debt is based on LIBOR or the prime rate and thus subject to adverse changes in market interest rates. Assuming there were no increases or decreases in the balance outstanding under our variable-rate debt at June 30, 2010, each hypothetical 100 basis points increase in interest rates would increase interest expense and decrease net income by approximately $748,000.

Our fixed-rate debt at June 30, 2010 was comprised of SBA debentures and structured notes of the 2000 Joint Venture.

The following tables present the principal amounts by year of expected maturity, weighted average interest rates and estimated fair values to evaluate the expected cash flows and sensitivity to interest rate changes of our outstanding debt at June 30, 2010 and December 31, 2009:

	Twelve Month Periods Ending June 30,						Carrying	Fair
	2011	2012	2013	2014	2015	Thereafter	Value	Value (1)
				(Dollars in thousands)				
Fixed-rate debt (2)	$ 1,894	$ 2,079	$ 2,341	$ 6,379	$ 6,238	$ 3,274	$ 22,205	$ 23,071
Variable-rate debt (LIBOR and prime based) (3) (4)	26,774	2,151	2,205	2,281	2,341	39,087	74,839	63,145
Totals	$28,668	$ 4,230	$ 4,546	$ 8,660	$ 8,579	$ 42,361	$ 97,044	$ 86,216

(1) *The estimated fair value is based on a present value calculation based on prices of the same or similar instruments after considering risk, current interest rates and remaining maturities.*

(2) *The weighted average interest rate of our fixed-rate debt at June 30, 2010 was 6.8%.*

(3) *Principal payments on the structured notes and secured borrowings are dependent upon cash flows received from the underlying loans. Our estimate of their repayment is based upon scheduled principal payments on the underlying loans. Our estimate will differ from actual amounts to the extent we experience prepayments and/or loan losses.*

(4) *The weighted average interest rate of our variable-rate debt at June 30, 2010 was 3.3%.*

	Years Ending December 31,							
	2010	2011	2012	2013	2014	Thereafter	Carrying Value	Fair Value (1)
	(Dollars in thousands)							
Fixed-rate debt (2)	$ 1,975	$ —	$ —	$ 4,173	$ —	$ 4,000	$ 10,148	$ 10,047
Variable-rate debt (LIBOR and prime rate based) (3)	24,239	1,294	1,343	1,366	1,425	28,694	58,361	45,817
Totals	$26,214	$ 1,294	$ 1,343	$ 5,539	$ 1,425	$ 32,694	$ 68,509	$ 55,864

(1) *The estimated fair value is based on a present value calculation based on prices of the same or similar instruments after considering risk, current interest rates and remaining maturities.*

(2) *The weighted average interest rate of our fixed-rate debt at December 31, 2009 was 6.2%.*

(3) *The weighted average interest rate of our variable-rate debt at December 31, 2009 was 3.3%.*

ITEM 4.
Controls and Procedures

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

Under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, management has evaluated the effectiveness of our disclosure controls and procedures (as defined under rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended) as of June 30, 2010. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There have been no changes in our internal control over financial reporting that occurred during the quarter ended June 30, 2010 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II
Other Information

ITEM 1. Legal Proceedings

In the normal course of business we are periodically party to certain legal actions and proceedings involving matters that are generally incidental to our business (*i.e.*, collection of loans receivable). In management's opinion, the resolution of these legal actions and proceedings will not have a material adverse effect on our consolidated financial statements.

ITEM 1A. Risk Factors

There have been no material changes to the factors disclosed in Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2009.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

ITEM 3. Defaults upon Senior Securities

None.

ITEM 4. Reserved

ITEM 5. Other Information

None.

ITEM 6. Exhibits

A. Exhibits

3.1	Declaration of Trust (incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-11 filed with the Securities and Exchange Commission ("SEC") on June 25, 1993, as amended (Registration No. 33-65910)).
3.1(a)	Amendment No. 1 to Declaration of Trust (incorporated by reference to the Registrant's Registration Statement on Form S-11 filed with the SEC on June 25, 1993, as amended (Registration No. 33-65910)).
3.1(b)	Amendment No. 2 to Declaration of Trust (incorporated by reference to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1993).
3.1(c)	Amendment No. 3 to Declaration of Trust (incorporated by reference to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2003).
3.2	Bylaws (incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-11 filed with the SEC on June 25, 1993, as amended (Registration No. 33-65910)).
3.3	Amendment No. 1 to Bylaws (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed with the SEC on April 16, 2009).
10.1	Form of Executive Employment Contract (incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on June 15, 2010).
*31.1	Section 302 Officer Certification — Chief Executive Officer
*31.2	Section 302 Officer Certification — Chief Financial Officer
**32.1	Section 906 Officer Certification — Chief Executive Officer
**32.2	Section 906 Officer Certification — Chief Financial Officer

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* Filed herewith.

** Submitted herewith

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 thereunto duly authorized.

PMC Commercial Trust

Date: 08/09/10

/s/ Lance B. Rosemore
Lance B. Rosemore
President and Chief Executive Officer

Date: 08/09/10

/s/ Barry N. Berlin
Barry N. Berlin
Executive Vice President and
Chief Financial Officer
(Principal Accounting Officer)

Exhibit 31.1

CERTIFICATION

I, Lance B. Rosemore, certify that:

1. I have reviewed this quarterly report on Form 10-Q of PMC Commercial Trust;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
   a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: 08/09/10

/s/ Lance B. Rosemore
Lance B. Rosemore
Chief Executive Officer

Exhibit 31.2

CERTIFICATION

I, Barry N. Berlin, certify that:

1. I have reviewed this quarterly report on Form 10-Q of PMC Commercial Trust;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
   a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: 08/09/10

/s/ Barry N. Berlin
Barry N. Berlin
Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of PMC Commercial Trust (the “Company”) on Form 10-Q for the period ended June 30, 2010 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Lance B. Rosemore, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Lance B. Rosemore
Lance B. Rosemore
Chief Executive Officer
August 9, 2010

EXHIBIT 32.2

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of PMC Commercial Trust (the “Company”) on Form 10-Q for the period ended June 30, 2010 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Barry N. Berlin, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Barry N. Berlin
Barry N. Berlin
Chief Financial Officer
August 9, 2010