

PMC COMMERCIAL TRUST /TX

Form 10-K

March 15, 2012

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10 K

(Mark One)

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

For the Fiscal Year Ended December 31, 2011

OR

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

For the Transition Period From to

Commission File Number: 1-13610

PMC COMMERCIAL TRUST

(Exact name of registrant as specified in its charter)

Texas
(State or other jurisdiction of

incorporation or organization)

75-6446078
(I.R.S. Employer

Identification No.)

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17950 Preston Road, Suite 600, Dallas, TX 75252
(Address of principal executive offices)

(972) 349-3200
(Registrant's telephone number)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common shares of beneficial interest, \$.01 par value	NYSE Amex

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark whether the Registrant is a well-known seasoned issuer (as defined in Rule 405 of the Securities Act). YES NO

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 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

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 NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 Accelerated filer

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

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

The aggregate market value of common shares held by non-affiliates of the Registrant, based upon the closing sale price of the Common Shares of Beneficial Interest on June 30, 2011 as reported on the NYSE Amex, was approximately \$82 million. Common Shares of Beneficial Interest held by each officer and trust manager and by each person who owns 10% or more of the outstanding Common Shares of Beneficial Interest have been excluded because such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of March 5, 2012, the Registrant had outstanding 10,574,554 Common Shares of Beneficial Interest.

DOCUMENTS INCORPORATED BY REFERENCE:

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Portions of the Registrant's Proxy Statement to be filed with the Securities and Exchange Commission within 120 days after the year covered by this Form 10-K with respect to the Annual Meeting of Shareholders are incorporated by reference into Part III of this Form 10-K.

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PMC COMMERCIAL TRUST

Form 10-K

For the Year Ended December 31, 2011

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Forward-Looking Statements

This Form 10-K 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. These statements include the plans and objectives of management for future operations, including plans and objectives relating to future growth of our loans receivable and availability of funds. 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. The forward-looking statements included herein are based on current expectations that involve numerous risks and uncertainties identified in this Form 10-K, including, without limitation, the risks identified under the caption Item 1A. Risk Factors. 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-K 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, except to the extent required by applicable securities laws.

PART I

Item 1. BUSINESS

INTRODUCTION

PMC Commercial Trust (PMC Commercial and together with its wholly-owned subsidiaries, the Company, our or we) is a real estate investment trust (REIT) organized in 1993 that primarily originates loans to small businesses collateralized by first liens on the real estate of the related business. As a REIT, we seek to maximize shareholder value through long-term growth in dividends paid to our shareholders. We must distribute at least 90% of our REIT taxable income to shareholders to maintain our REIT status. See Tax Status. Our common shares are traded on the NYSE Amex under the symbol PCC.

We generate revenue primarily from the yield and other fees earned on our investments. Our loans are predominantly (93.5% at December 31, 2011) to borrowers in the hospitality industry. Our operations are located in Dallas, Texas and include originating, servicing and selling the government guaranteed portions of certain loans. During the years ended December 31, 2011 and 2010, our total revenues were approximately \$16.1 million and \$15.5 million, respectively, and our net income was approximately \$3.6 million and \$4.3 million, respectively. See Item 8. Financial Statements and Supplementary Data.

We originate loans through PMC Commercial and its wholly-owned lending subsidiaries: First Western SBLC, Inc. (First Western), PMC Investment Corporation (PMCIC) and Western Financial Capital Corporation (Western Financial). First Western is licensed as a small business lending company (SBLC) that originates loans through the Small Business Administration s (SBA) 7(a) Guaranteed Loan Program (SBA 7(a) Program). PMCIC and Western Financial are licensed small business investment companies (SBICs).

First Western is a national Preferred Lender, as designated by the SBA, and originates, sells and services small business loans. As a non-bank SBA 7(a) Program lender, First Western is able to originate loans on which a substantial portion of the loan (generally 75% to 85%) is guaranteed as to payment of principal and interest by the SBA. Due to the existence of the SBA guarantee, we are able to originate loans that meet the criteria of the SBA 7(a) Program and have less stringent underwriting criteria than our non-SBA 7(a) Program loan originations. See Lending Activities SBA Programs.

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, primarily secured by real estate, and then sell the government guaranteed portion to investors.

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Our ability to generate interest income, as well as other revenue sources, is dependent on economic, regulatory and competitive factors that influence interest rates and loan originations, and our ability to secure financing for our investment activities. The amount of revenue recorded will vary from current levels based on a number of factors including, but not limited to:

The volume of loans funded;

The volume of loans which prepay;

The timing and availability of leverage;

The amount of non-performing loans;

Recognition of premium income, if any, on secondary market loan sales depending on the type of sale;

The interest rate and type of loans originated (whether fixed or variable); and

The general level of interest rates.

The majority of our loans (81% at December 31, 2011) have variable rates of interest. As a result, during periods of declining interest rates, our interest income is subject to interest rate risk. See Item 7a. Quantitative and Qualitative Disclosures About Market Risk.

Generally, in order to fund new loans, we need to borrow funds or sell loans. Since 2006, our working capital was primarily provided through credit facilities and principal payments (including prepayments) on loans receivable. Prior to 2006, our primary source of long-term funds was structured loan sale transactions and the issuance of junior subordinated notes. At the current time, there is a limited market for structured loan sale transactions (more commonly known as securitizations) and there is no market for the issuance of trust preferred securities (junior subordinated notes). We cannot anticipate when, or if, these markets will be available to us. Until these markets become available or alternative debt and/or equity structures become available, our ability to grow is limited. Due to (1) the lack of a market for our type of securitization and the prospect that this market may never recover to its prior form or may return with costs or structures that we may not be able to accept and (2) limits on the amounts of capital available through credit or warehouse facilities, we continue to focus our lending activities on originating loans under the SBA 7(a) Program.

LENDING ACTIVITIES

Overview

We are a national lender that primarily originates loans to small businesses, principally in the limited service hospitality industry. In addition to first liens on the real estate of the related business, our loans are typically personally guaranteed by the principals of the entities obligated on the loans.

We identify loan origination opportunities through personal contacts, internet referrals, attendance at trade shows and meetings, direct mailings, advertisements in trade publications and other marketing methods. We also generate loans through referrals from real estate and loan brokers, franchise representatives, existing borrowers, lawyers and accountants. Payments are sometimes made to non-affiliated individuals who assist in generating loan applications, with such payments generally not exceeding 1% of the principal amount of the originated loan.

Limited Service Hospitality Industry

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Our outstanding loans are generally collateralized by first liens on limited service hospitality properties and are typically for owner-operated facilities operating under national franchises, including, among others, Comfort Inn, Days Inn, Holiday Inn Express, Ramada and Best Western. We believe that franchise operations offer attractive lending opportunities because such businesses generally employ proven business concepts, have national reservation systems and advertising, consistent product quality, are screened and monitored by franchisors and generally have a higher rate of success when compared to other independently operated hospitality businesses.

Loan Originations and Underwriting

We believe that we successfully compete in certain sectors of the commercial real estate finance market, primarily the limited service hospitality sector, due to our diligent underwriting which is benefitted by our understanding of our borrowers' businesses and our responsive customer service.

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We consider traditional underwriting criteria such as:

The underlying cash flow of the owner-operator;

The components, value and replacement cost of the borrower's collateral (primarily real estate);

The industry and competitive environment in which the borrower operates;

The financial strength of the guarantors;

Analysis of local market conditions;

The ease with which the collateral can be liquidated;

The existence of any secondary repayment sources;

Evaluation of the property operator; and

The existence of a franchise relationship.

Upon receipt of a completed loan application, our credit department conducts: (1) a detailed analysis of the potential loan, which typically includes a third-party licensed appraisal and a valuation by our credit department of the property that will collateralize the loan to ensure compliance with loan-to-value percentages, (2) a site inspection for real estate collateralized loans, (3) a review of the borrower's business experience, (4) a review of the borrower's credit history, and (5) an analysis of the borrower's debt-service-coverage, debt-to-equity and other applicable ratios. We also utilize local market economic information to the extent available.

We believe that our typical non-SBA 7(a) Program loan is distinguished from those of some of our competitors by the following characteristics:

Substantial down payments are required. We usually require an initial down payment of not less than 20% of the total cost of the project being financed. Our experience has shown that the likelihood of full repayment of a loan increases if the owner/operator is required to make an initial and substantial financial commitment to the project being financed.

Cash outs are typically not permitted. Generally, we will not make a loan in an amount greater than the lesser of 80% of either the replacement cost or current appraised value of the property which is collateral for the loan. For example, a hotel property may have been originally constructed for a cost of \$2.0 million, with the owner/operator initially borrowing \$1.6 million of that amount. At the time of the borrower's loan refinancing request, the property securing the loan is appraised at \$4.0 million. Some of our competitors might loan from 70% to 90% or more of the new appraised value of the property and permit the owner/operator to receive a cash distribution from the proceeds. Generally, we would not permit this type of cash-out distribution.

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The obligor is personally liable for the loan. We typically require the principals of the borrower to personally guarantee the loan.

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Interest rates on our loans receivable, net, were as follows:

	September 30, 2011	September 30, 2011	September 30, At December 31, 2010	September 30, 2010	September 30, 2010	September 30, 2010
	Loans Receivable, net Amount	%	Weighted Average Interest Rate (Dollars in thousands)	Loans Receivable, net Amount	%	Weighted Average Interest Rate
Variable-rate - LIBOR	\$ 132,596	56.6%	4.4%	\$ 125,606	53.9%	4.2%
Variable-rate - prime	57,338	24.4%	5.8%	44,349	19.0%	5.7%
Fixed-rate	44,493	19.0%	9.2%	63,263	27.1%	9.1%
Total	\$ 234,427	100.0%	5.6%	\$ 233,218	100.0%	5.8%

Our variable-rate loans generally require monthly payments of principal and interest, reset on a quarterly basis, to amortize the principal over the remaining life of the loan. Fixed-rate loans generally require level monthly payments of principal and interest calculated to amortize the principal over the remaining life of the loan.

Industry Concentration

The distribution of our loans receivable by industry was as follows at December 31, 2011:

	September 30, Number of Loans	September 30, Cost (1) (Dollars in thousands)	September 30, % of Total Cost
Hotels and motels	240	\$ 220,896	93.5%
Convenience stores/service stations	16	8,740	3.7%
Services	18	1,549	0.7%
Restaurants	23	661	0.3%
Retail	6	397	0.2%
Other	21	3,872	1.6%
	324	\$ 236,115	100.0%

(1) Loan portfolio outstanding before loan loss reserves and deferred commitment fees.

Table of Contents**Loan Portfolio Statistics**

Information on our loans receivable was as follows:

	September 30, At December 31, 2011	September 30, 2010
	<i>(Dollars in thousands)</i>	
Principal outstanding (1)	\$ 236,115	\$ 234,867
Weighted average interest rate	5.6%	5.8%
Average yield (2)	5.8%	5.8%
Weighted average contractual maturity in years	15.0	14.9
Hospitality industry concentration	93.5%	93.8%
Texas concentration (3)	18.1%	19.5%

(1) Loans receivable outstanding before loan loss reserves and deferred commitment fees.

(2) The calculation of average yield divides our interest income, prepayment fees and other loan related fees, adjusted by the provision for loan losses, by the weighted average loans receivable outstanding.

(3) No other state concentrations greater than or equal to 10% existed at December 31, 2011 or 2010.

Loans Funded

The following table is a breakdown of loans funded during the years indicated:

	September 30, 2011	September 30, 2010	September 30, Years Ended December 31, 2009	September 30, 2008	September 30, 2007
	<i>(In thousands)</i>				
Commercial mortgage loans	\$ 4,680	\$ 4,908	\$ 2,425	\$ 19,739	\$ 28,416
SBA 7(a) Program loans	33,672	33,532	28,010	10,971	2,888
SBA 504 Program loans (1)				3,877	2,452
Total loans funded	\$ 38,352	\$ 38,440	\$ 30,435	\$ 34,587	\$ 33,756

(1) Represents second mortgages originated through the SBA 504 Program which were repaid by certified development companies.

Secondary Market Loan Sales

Our SBA 7(a) subsidiary sells loans pursuant to the SBA 7(a) Program. The SBA guaranteed portions of these loans are sold in legal sale transactions to either dealers in government guaranteed loans or institutional investors (Secondary Market Loan Sales) as the loans are fully funded. These government guaranteed portions of loans may be sold for (1) a cash premium and the minimum 1% required servicing spread, (2) significant future servicing spread and no cash premium or (3) future servicing spread and a cash premium of 10% (hybrid loan sales). Prior to January 1, 2010, all of these types of transactions were recorded as sales (*i.e.*, we recorded premium income) for accounting purposes. Effective January 1, 2010, due to a change in accounting rules, we were required to permanently treat certain of the proceeds received from these

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legally sold portions of loans (those loans sold solely for future servicing spread and those loans sold for a cash premium of 10% and future servicing spread) as secured borrowings (debt) for the life of the loan and 100% of the loan is included in our loans receivable. We can no longer record premium income on these types of sales. Cash premiums collected on hybrid loan sales are deferred and reflected as a liability on our consolidated balance sheet and amortized as a reduction to interest expense over the life of the loan. Deferred cash premiums at December 31, 2011 were \$2.4 million.

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SBA Programs

General

We utilize programs established by the SBA to generate loan origination opportunities and provide us with a funding source as follows:

We have an SBLC that originates loans through the SBA 7(a) Program;

We have participated as a private lender in the SBA 504 Program which allowed us to originate first mortgage loans with lower loan-to-value ratios;

We have two licensed SBICs regulated under the Small Business Investment Act of 1958, as amended. Our SBICs use long-term funds provided by the SBA, together with their own capital, to provide long-term collateralized loans to eligible small businesses, as defined under SBA regulations.

Our regulated SBA subsidiaries are periodically examined and audited by the SBA to determine compliance with SBA regulations.

SBA 7(a) Program

Under the SBA 7(a) Program, the SBA typically guarantees 75% of qualified loans over \$150,000. While the eligibility requirements of the SBA 7(a) Program vary by the industry of the borrower and other factors, the general eligibility requirements include, but are not limited to: (1) gross sales of the borrower cannot exceed size standards set by the SBA (*i.e.*, \$7.0 million for limited service hospitality properties) or alternatively average net income cannot exceed \$5 million for the most recent two fiscal years, (2) liquid assets of the borrower and affiliates cannot exceed specified limits, (3) tangible net worth of the borrower must be less than \$15 million, (4) the borrower must be a U.S. citizen and (5) the maximum aggregate SBA loan guarantees to a borrower cannot exceed \$3.75 million. Maximum maturities for SBA 7(a) Program loans are 25 years for real estate and between seven and 10 years for the purchase of machinery, furniture, fixtures and/or equipment. In order to operate as an SBLC, a licensee is required to maintain a minimum regulatory capital (as defined by SBA regulations) of the greater of (1) 10% of its outstanding loans receivable and other investments or (2) \$1.0 million, and is subject to certain other regulatory restrictions such as change in control provisions. See Item 1A. Risk Factors.

SBIC Program

We originate loans to small businesses through our SBICs. According to SBA regulations, SBICs may make long-term loans to small businesses and invest in the equity securities of such businesses. Under SBA regulations, eligible small businesses include those that have a net worth not exceeding \$18 million and have average annual fully taxable net income not exceeding \$6 million for the most recent two fiscal years. To the extent approved, an SBIC can issue debentures whose principal and interest is guaranteed to be paid to the debt holder in the event of non-payment by the SBIC. As a result, the debentures' costs of funds are usually lower compared to alternative fixed-rate sources of funds available to us.

SBA 504 Program

The SBA 504 Program assists small businesses in obtaining subordinated, long-term financing by guaranteeing debentures available through certified development companies (CDCs) for the purpose of acquiring land, building, machinery and equipment and for modernizing, renovating or restoring existing facilities and sites. A typical finance structure for an SBA 504 Program project would include a first mortgage covering 50% of the project cost from a private lender, a second mortgage obtained from a CDC covering up to 40% of the project cost and a contribution of at least 10% of the project cost by the principals of the small businesses being assisted. We typically require at least a 20% contribution of the equity in a project by our borrowers. The SBA does not guarantee the first mortgage. Although the total sizes of projects utilizing the SBA 504 Program are unlimited, currently the maximum amount of subordinated debt in any individual project is generally \$5 million (or \$5.5 million for certain projects). Typical project costs range in size from \$1 million to \$6 million. Our SBA 504 Program has been inactive since the beginning of 2008 due to our limited liquidity.

TAX STATUS

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PMC Commercial has elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended (the Code). As a REIT, PMC Commercial is generally not subject to Federal income tax (including any applicable alternative minimum tax) to the extent that it distributes at least 90% of its REIT taxable income to shareholders. Certain of PMC Commercial's subsidiaries, including First Western and PMCIC, have elected to be treated as taxable REIT subsidiaries; thus, their earnings are subject to U.S. Federal income tax. To the extent PMC Commercial's taxable REIT subsidiaries retain their earnings and profits, these earnings and profits will be unavailable for distribution to our shareholders.

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PMC Commercial may, however, be subject to certain Federal excise taxes and state and local taxes on its income and property. If PMC Commercial fails to qualify as a REIT in any taxable year, it will be subject to Federal income taxes at regular corporate rates (including any applicable alternative minimum tax) and will not be able to qualify as a REIT for four subsequent taxable years. REITs are subject to a number of organizational and operational requirements under the Code. See Item 1A. Risk Factors REIT Related Risks for additional tax status information.

EMPLOYEES

We employed 33 individuals including marketing professionals, investment professionals, operations professionals and administrative staff as of December 31, 2011. We have employment agreements with our executive officers. Our operations are centralized in Dallas, Texas. We believe the relationship with our employees is good.

COMPETITION

When originating loans we compete with other specialty commercial lenders, banks, broker dealers, other REITs, savings and loan associations, insurance companies and other entities that originat