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

Form 10-Q

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

For the quarterly period ended June 30, 2008

or

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

For the transition period from _____ to _____

Commission file number: 001-32136

Arbor Realty Trust, Inc.

(Exact name of registrant as specified in its charter)

Maryland
*(State or other jurisdiction of
incorporation)*

**333 Earle Ovington Boulevard, Suite 900
Uniondale, NY**
(Address of principal executive offices)

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

11553
Zip Code

(516) 832-8002

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant 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 Smaller reporting company
(Do not check if a smaller reporting company)

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. Common stock, \$0.01 par value per share: 24,737,696 outstanding (excluding 279,400 shares held in the treasury) as of July 31, 2008.

ARBOR REALTY TRUST, INC.

FORM 10-Q
INDEX

<u>PART I. FINANCIAL INFORMATION</u>	2
<u>Item 1. Financial Statements</u>	2
<u>Consolidated Balance Sheets at June 30, 2008 (Unaudited) and December 31, 2007</u>	2
<u>Consolidated Income Statements (Unaudited) for the Three and Six Months Ended June 30, 2008 and 2007</u>	3
<u>Consolidated Statements of Stockholders' Equity (Unaudited) for the Six Months Ended June 30, 2008</u>	4
<u>Consolidated Statements of Cash Flows (Unaudited) for the Six Months Ended June 30, 2008 and 2007</u>	5
<u>Notes to the Consolidated Statements (Unaudited)</u>	6
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	33
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	51
<u>Item 4. Controls and Procedures</u>	54
<u>PART II. OTHER INFORMATION</u>	54
<u>Item 1. Legal Proceedings</u>	54
<u>Item 1A. Risk Factors</u>	54
<u>Item 2. Unregistered Sale of Equity Securities and Use of Proceeds</u>	54
<u>Item 3. Defaults Upon Senior Securities</u>	54
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	55
<u>Item 5. Other Information</u>	56
<u>Item 6. Exhibits</u>	56
<u>Signatures</u>	59
<u>EX-10.28: SECOND AMENDMENT MANAGEMENT AND ADVISORY AGREEMENT</u>	
<u>EX-10.29: AMENDMENT NO. 2 TO OMNIBUS STOCK INCENTIVE PLAN</u>	
<u>EX-10.30: AMENDMENT NO. 3 TO OMNIBUS STOCK INCENTIVE PLAN</u>	
<u>EX-31.1: CERTIFICATION</u>	
<u>EX-31.2: CERTIFICATION</u>	
<u>EX-32.1: CERTIFICATION</u>	
<u>EX-32.2: CERTIFICATION</u>	

CAUTIONARY STATEMENTS

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

This report contains certain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements relate to, among other things, the operating performance of our investments and financing needs. Forward-looking statements are generally identifiable by use of forward-looking terminology such as “may,” “will,” “should,” “potential,” “intend,” “expect,” “endeavor,” “seek,” “anticipate,” “estimate,” “overestimate,” “underestimate,” “believe,” “could,” “project,” “predict,” “continue” or other similar words or expressions. Forward-looking statements are based on certain assumptions, discuss future expectations, describe future plans and strategies, contain projections of results of operations or of financial condition or state other forward-looking information. Our ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Although we believe that the expectations reflected in such forward-looking statements are based on reasonable assumptions, our actual results and performance could differ materially from those set forth in the forward-looking statements. These forward-looking statements involve risks, uncertainties and other factors that may cause our actual results in future periods to differ materially from forecasted results. Factors that could have a material adverse effect on our operations and future prospects include, but are not limited to, changes in economic conditions generally and the real estate market specifically; adverse changes in the financing markets we access affecting our ability to finance our loan and investment portfolio; changes in interest rates; the quality and size of the investment pipeline and the rate at which we can invest our cash; impairments in the value of the collateral underlying our loans and investments; changes in the markets; legislative/regulatory changes; completion of pending investments; the availability and cost of capital for future investments; competition within the finance and real estate industries; and other risks detailed in our Annual Report on Form 10-K for the year ending December 31, 2007. Readers are cautioned not to place undue reliance on any of these forward-looking statements, which reflect our management’s views as of the date of this report. The factors noted above could cause our actual results to differ significantly from those contained in any forward-looking statement. For a discussion of our critical accounting policies, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations of Arbor Realty Trust, Inc. and Subsidiaries — Significant Accounting Estimates and Critical Accounting Policies” in our Annual Report on Form 10-K for the year ending December 31, 2007.

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

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

	<u>June 30, 2008</u>	<u>December 31, 2007</u>
	(Unaudited)	
Assets:		
Cash and cash equivalents	\$ 46,195,338	\$ 22,219,541
Restricted cash	144,099,637	139,136,105
Loans and investments, net	2,444,641,847	2,592,093,930
Available-for-sale securities, at fair value	10,111,759	15,696,743
Securities held-to-maturity, net	58,498,406	—
Investment in equity affiliates	28,850,691	29,590,190
Real estate owned, net	46,891,971	—
Deferred management fee — related party	7,292,448	—
Prepaid management fee — related party	19,047,949	19,047,949
Other assets	96,439,720	83,709,076
Total assets	<u>\$2,902,069,766</u>	<u>\$2,901,493,534</u>
Liabilities and Stockholders' Equity:		
Repurchase agreements	\$ 198,755,637	\$ 244,937,929
Collateralized debt obligations	1,129,649,000	1,151,009,000
Junior subordinated notes to subsidiary trust issuing preferred securities	276,055,000	276,055,000
Notes payable	635,388,432	596,160,338
Mortgage note payable	41,440,000	—
Due to related party	7,914,458	2,429,109
Due to borrowers	8,392,612	18,265,906
Deferred revenue	77,123,133	77,123,133
Other liabilities	58,172,508	67,395,776
Total liabilities	<u>2,432,890,780</u>	<u>2,433,376,191</u>
Minority interest	—	72,854,258
Stockholders' equity:		
Preferred stock, \$0.01 par value: 100,000,000 shares authorized; 0 shares issued and outstanding at June 30, 2008 and 3,776,069 shares issued and outstanding at December 31, 2007	—	37,761
Common stock, \$0.01 par value: 500,000,000 shares authorized; 25,017,096 shares issued, 24,737,696 shares outstanding at June 30, 2008 and 20,798,735 shares issued, 20,519,335 shares outstanding at December 31, 2007	250,171	207,987
Additional paid-in capital	442,592,734	365,376,136
Treasury stock, at cost — 279,400 shares	(7,023,361)	(7,023,361)
Retained earnings	64,362,458	65,665,951
Accumulated other comprehensive loss	(31,003,016)	(29,001,389)
Total stockholders' equity	<u>469,178,986</u>	<u>395,263,085</u>
Total liabilities and stockholders' equity	<u>\$2,902,069,766</u>	<u>\$2,901,493,534</u>

See notes to consolidated financial statements.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES

CONSOLIDATED INCOME STATEMENTS

For the Three and Six Months Ended June 30, 2008 and 2007
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Revenue:				
Interest income	\$51,869,164	\$74,800,274	\$107,285,494	\$141,260,927
Other income	28,629	17,186	49,322	23,356
Total revenue	<u>51,897,793</u>	<u>74,817,460</u>	<u>107,334,816</u>	<u>141,284,283</u>
Expenses:				
Interest expense	27,857,322	38,527,983	59,161,421	70,640,502
Employee compensation and benefits	2,686,002	2,753,662	4,663,345	4,484,017
Selling and administrative	2,793,161	1,593,494	4,331,227	2,814,866
Provision for loan losses	2,000,000	—	5,000,000	—
Management fee — related party	2,153,838	10,645,065	4,733,272	15,518,747
Total expenses	<u>37,490,323</u>	<u>53,520,204</u>	<u>77,889,265</u>	<u>93,458,132</u>
Income before income from equity affiliates, minority interest and provision for income taxes	14,407,470	21,297,256	29,445,551	47,826,151
(Loss) income from equity affiliates	(562,000)	26,025,788	(562,000)	26,025,788
Income before minority interest and provision for income taxes	13,845,470	47,323,044	28,883,551	73,851,939
Income allocated to minority interest	2,117,464	6,638,020	4,450,754	10,318,334
Income before provision for income taxes	11,728,006	40,685,024	24,432,797	63,533,605
Provision for income taxes	—	9,000,000	—	15,085,000
Net income	<u>\$11,728,006</u>	<u>\$31,685,024</u>	<u>\$ 24,432,797</u>	<u>\$ 48,448,605</u>
Basic earnings per common share	<u>\$ 0.56</u>	<u>\$ 1.76</u>	<u>\$ 1.18</u>	<u>\$ 2.75</u>
Diluted earnings per common share	<u>\$ 0.56</u>	<u>\$ 1.75</u>	<u>\$ 1.18</u>	<u>\$ 2.74</u>
Dividends declared per common share	<u>\$ 0.62</u>	<u>\$ 0.62</u>	<u>\$ 1.24</u>	<u>\$ 1.22</u>
Weighted average number of shares of common stock outstanding:				
Basic	<u>20,906,383</u>	<u>17,993,924</u>	<u>20,739,081</u>	<u>17,590,860</u>
Diluted	<u>24,721,660</u>	<u>21,873,322</u>	<u>24,562,520</u>	<u>21,453,969</u>

See notes to consolidated financial statements.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
For the Six Months Ended June 30, 2008
(Unaudited)

	Comprehensive Loss	Preferred Stock Shares	Preferred Stock Par Value	Common Stock Shares	Common Stock Par Value	Additional Paid-in Capital	Treasury Stock Shares	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance — January 1, 2008	\$ —	3,776,069	\$ 37,761	20,798,735	\$207,987	\$365,376,136	(279,400)	\$(7,023,361)	\$ 65,665,951	\$ (29,001,389)	\$395,263,085
Issuance of common stock for management incentive fee				142,304	1,423	2,233,890					2,235,313
Redemption of operating partnership units for common stock		(3,776,069)	(37,761)	3,776,069	37,761	67,306,291					67,306,291
Deferred compensation				300,740	3,008	(3,008)					—
Forfeit unvested restricted stock				(752)	(8)	8					—
Stock based compensation						2,363,022					2,363,022
Distributions— common stock									(25,736,290)		(25,736,290)
Adjustment to minority interest from decreased ownership in ARLP						5,316,395					5,316,395
Net income	24,432,797								24,432,797		24,432,797
Net unrealized loss on securities available for sale	(5,584,985)									(5,584,985)	(5,584,985)
Unrealized gain on derivative financial instruments	3,583,358									3,583,358	3,583,358
Balance — June 30, 2008	\$ 22,431,170	—	\$ —	25,017,096	\$250,171	\$442,592,734	(279,400)	\$(7,023,361)	\$ 64,362,458	\$ (31,003,016)	\$469,178,986

See notes to consolidated financial statements.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Six Months Ended June 30, 2008 and 2007
(Unaudited)

	For the Six Months Ended	
	June 30,	
	2008	2007
Operating activities:		
Net income	\$ 24,432,797	\$ 48,448,605
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation	170,913	—
Stock based compensation	2,055,922	1,673,936
Provision for loan losses	5,000,000	—
Minority interest	4,450,754	10,318,334
Amortization and accretion of interest	318,889	(556,998)
Non-cash incentive compensation to manager — related party	1,385,918	14,083,102
Loss (earnings) from equity affiliates	562,000	(24,150,787)
Gain on sales of securities available for sale	—	(30,182)
Changes in operating assets and liabilities:		
Other assets	(12,471,981)	(1,925,335)
Deferred revenue	—	77,123,133
Other liabilities	(13,465,899)	20,475,129
Deferred origination fees	447	(65,465)
Due to related party	(957,704)	374,261
Net cash provided by operating activities	<u>\$ 11,482,056</u>	<u>\$ 145,767,733</u>
Investing activities:		
Loans and investments originated and purchased, net	(287,005,064)	(1,444,636,554)
Payoffs and paydowns of loans and investments	427,986,599	888,153,140
Due to borrowers	(9,873,294)	7,697,163
Purchases of securities held—to—maturity	(58,062,500)	—
Investment in real estate, net	(1,073,153)	—
Prepayments on securities available—for—sale	—	3,358,184
Proceeds from sales of securities available for sale	—	18,792,594
Change in restricted cash	(4,963,532)	(113,778,067)
Contributions to equity affiliates	—	(6,928,826)
Distributions from equity affiliates	177,499	12,210,938
Net cash provided by/(used in) investing activities	<u>\$ 67,186,555</u>	<u>\$ (635,131,428)</u>
Financing activities:		
Proceeds from notes payable and repurchase agreements	212,693,265	766,442,235
Payoffs and paydowns of notes payable and repurchase agreements	(219,647,463)	(423,222,570)
Proceeds from collateralized debt obligations	27,000,000	55,700,000
Payoffs and paydowns of collateralized debt obligations	(48,360,000)	(6,360,000)
Payments on swaps to hedge counterparties	(79,770,000)	—
Receipts on swaps from hedge counterparties	83,810,000	—
Proceeds from issuance of junior subordinated notes	—	53,093,000
Proceeds from sale of common stock	—	74,655,000
Offering expenses paid	—	(953,932)
Distributions paid to minority interest	(4,682,326)	(4,606,804)
Distributions paid on common stock	(25,736,290)	(21,183,959)
Payment of deferred financing costs	—	(2,009,548)
Net cash (used in)/provided by financing activities	<u>\$ (54,692,814)</u>	<u>\$ 491,553,422</u>
Net increase in cash and cash equivalents	<u>\$ 23,975,797</u>	<u>\$ 2,189,727</u>
Cash and cash equivalents at beginning of period	<u>22,219,541</u>	<u>7,756,857</u>
Cash and cash equivalents at end of period	<u>\$ 46,195,338</u>	<u>\$ 9,946,584</u>
Supplemental cash flow information:		
Cash used to pay interest, net of capitalized interest	<u>\$ 60,253,699</u>	<u>\$ 70,727,001</u>
Cash used to pay taxes	<u>\$ 57,160</u>	<u>\$ 178,021</u>
Supplemental schedule of non-cash financing activities:		
Collateral on swaps to hedge counterparties	<u>\$ 3,500,000</u>	<u>\$ —</u>
Accrued offering expenses	<u>\$ —</u>	<u>\$ 75,000</u>
Assumption of mortgage note payable	<u>\$ 41,440,000</u>	<u>\$ —</u>
Redemption of operating partnership units for common stock	<u>\$ 67,306,291</u>	<u>\$ —</u>

See notes to consolidated financial statements.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

Note 1 —Description of Business/Form of Ownership

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

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

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

On July 1, 2003, Arbor Commercial Mortgage, LLC (“ACM”) contributed \$213.1 million of structured finance assets and \$169.2 million of borrowings supported by \$43.9 million of equity in exchange for a commensurate equity ownership in ARLP. In addition, certain employees of ACM were transferred to ARLP. These assets, liabilities and employees represent a substantial portion of ACM’s structured finance business (the “SF Business”). The Company is externally managed and advised by ACM and pays ACM a management fee in accordance with a management agreement. ACM also sources originations, provides underwriting services and services all structured finance assets on behalf of ARLP, and its wholly owned subsidiaries.

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

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

On March 2, 2007, the Company filed a shelf registration statement on Form S-3 with the SEC under the Securities Act of 1933, as amended (the “1933 Act”) with respect to an aggregate of \$500.0 million of debt securities, common stock, preferred stock, depositary shares and warrants, that may be sold by the Company from time to time pursuant to Rule 415 of the 1933 Act. On April 19, 2007, the Commission declared this shelf registration statement effective.

In June 2007, the Company completed a public offering in which it sold 2,700,000 shares of its common stock registered for \$27.65 per share, and received net proceeds of approximately \$73.6 million after deducting the

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

underwriting discount and the other estimated offering expenses. The Company used the proceeds to pay down debt and finance its loan and investment portfolio. The underwriters did not exercise their over allotment option for additional shares. At June 30, 2008, the Company had \$425.3 million remaining under this shelf registration.

In June 2008, the Company's external manager, exercised its right to redeem its approximate 3.8 million operating partnership units in the Company's operating partnership for shares of the Company's common stock on a one-for-one basis. In addition, the special voting preferred shares paired with each operating partnership unit, pursuant to a pairing agreement, were redeemed simultaneously and cancelled by the Company.

The Company had 24,737,696 shares outstanding at June 30, 2008 and 20,519,335 shares outstanding at December 31, 2007.

Note 2 — Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

The accompanying unaudited consolidated interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial statements and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements, although management believes that the disclosures presented herein are adequate to make the accompanying unaudited consolidated interim financial statements presented not misleading.

The accompanying unaudited consolidated financial statements include the financial statements of the Company, its wholly owned subsidiaries, and partnerships or other joint ventures which the Company controls. Entities which the Company does not control and entities which are variable interest entities in which the Company is not the primary beneficiary, are accounted for under the equity method. In the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included. All significant inter-company transactions and balances have been eliminated in consolidation. Certain prior year amounts have been reclassified to conform to current period presentation. Stock based compensation was disclosed in the Company's Consolidated Income Statement under "employee compensation and benefits" for employees and under "selling and administrative" expense for non-employees in the current year presentation and disclosed as a separate line item in prior years presentation.

The preparation of consolidated interim financial statements in conformity with U.S. Generally Accepted Accounting Principals ("GAAP") requires management to make estimates and assumptions in determining the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated interim financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

The results of operations for the three and six months ended June 30, 2008 are not necessarily indicative of results that may be expected for the entire year ending December 31, 2008. The accompanying unaudited consolidated interim financial statements should be read in conjunction with the Company's audited consolidated annual financial statements and the related Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

Cash and Cash Equivalents

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

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

Restricted Cash

On June 30, 2008 and December 31, 2007, the Company had restricted cash of \$144.1 million and \$139.1 million, respectively, on deposit with the trustees for the Company's collateralized debt obligations ("CDOs"), see Note 6 "Debt Obligations." Restricted cash primarily represents proceeds from loan repayments which will be used to purchase replacement loans as collateral for the CDOs and interest payments received from loans in the CDOs which are remitted to the Company quarterly in the month following the quarter.

Loans and Investments

Statement of Financial Accounting Standards ("SFAS") No. 115 "Accounting for Certain Investments in Debt and Equity Securities," ("SFAS 115") requires that at the time of purchase, the Company designate a security as held to maturity, available for sale, or trading depending on ability and intent. Securities available for sale are reported at fair value, while securities and investments held to maturity are reported at amortized cost. The Company does not have any trading securities at this time.

Loans held for investment are intended to be held to maturity and, accordingly, are carried at cost, net of unamortized loan origination costs and fees, loan purchase discounts, and net of the allowance for loan losses when such loan or investment is deemed to be impaired. The Company invests in preferred equity interests that, in some cases, allow the Company to participate in a percentage of the underlying property's cash flows from operations and proceeds from a sale or refinancing. At the inception of each such investment, management must determine whether such investment should be accounted for as a loan, joint venture or as real estate. To date, management has determined that all such investments are properly accounted for and reported as loans.

The Company considers a loan impaired when, based upon current information and events, it is probable that it will be unable to collect all amounts due for both principal and interest according to the contractual terms of the loan agreement. Specific valuation allowances are established for impaired loans based on the fair value of collateral on an individual loan basis. The fair value of the collateral is determined by selecting the most appropriate valuation methodology, or methodologies, among several generally available and accepted in the commercial real estate industry. The determination of the most appropriate valuation methodology is based on the key characteristics of the collateral type. These methodologies include the evaluation of operating cash flow from the property during the projected holding period, and the estimated sales value of the collateral computed by applying an expected capitalization rate to the stabilized net operating income of the specific property, less selling costs, discounted at market discount rates.

If upon completion of the valuation, the fair value of the underlying collateral securing the impaired loan is less than the net carrying value of the loan, an allowance is created with a corresponding charge to the provision for loan losses. The allowance for each loan is maintained at a level believed adequate by management to absorb probable losses. The Company had an allowance for loan losses of \$3.5 million relating to three loans with an aggregate outstanding principal balance of approximately \$75.2 million at June 30, 2008 and \$2.5 million in allowance for loan losses relating to two loans with an aggregate outstanding principal balance of approximately \$58.5 million at December 31, 2007.

Capitalized Interest

The Company capitalizes interest in accordance with SFAS No. 58 "Capitalization of Interest Costs in Financial Statements that Include Investments Accounted for by the Equity Method." This statement amended SFAS No. 34 "Capitalization of Interest Costs" ("SFAS 34") to include investments (equity, loans and advances) accounted for by the equity method as qualifying assets of the investor while the investee has activities in progress necessary to commence its planned principal operations, provided that the investee's activities include the use of funds to acquire qualifying assets for its operations. One of the Company's joint ventures, which is accounted for using the equity method, has used funds to acquire qualifying assets for its planned principal operations. During 2007 the joint venture sold both of the acquired properties and the Company discontinued the capitalization of interest on its remaining investment in the joint venture as activities required under SFAS 34 ceased to continue.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

The Company capitalized \$0 and \$0.3 million of interest relating to this investment during the three and six months ended June 30, 2007. The Company did not capitalize interest during the three and six months ended June 30, 2008.

Revenue Recognition

Interest income is recognized on the accrual basis as it is earned from loans, investments, and securities. In many instances, the borrower pays an additional amount of interest at the time the loan is closed, an origination fee, and deferred interest upon maturity. In some cases interest income may also include the amortization or accretion of premiums and discounts arising from the purchase or origination of the loan or security. This additional income, net of any direct loan origination costs incurred, is deferred and accreted into interest income on an effective yield or “interest” method adjusted for actual prepayment activity over the life of the related loan or security as a yield adjustment. Income recognition is suspended for loans when in the opinion of management a full recovery of income and principal becomes doubtful. Income recognition is resumed when the loan becomes contractually current and performance is demonstrated to be resumed.

Several of the loans provide for accrual of interest at specified rates, which differ from current payment terms. Interest is recognized on such loans at the accrual rate subject to management’s determination that accrued interest and outstanding principal are ultimately collectible, based on the underlying collateral and operations of the borrower. If management cannot make this determination regarding collectibility, interest income above the current pay rate is recognized only upon actual receipt. Additionally, interest income is recorded when earned from equity participation interests, referred to as equity kickers. These equity kickers have the potential to generate additional revenues to the Company as a result of excess cash flows being distributed and/or as appreciated properties are sold or refinanced. The Company recorded interest on such loans and investments of \$0.3 million for the six months ended June 30, 2008, compared to \$23.0 million for the six months ended June 30, 2007. For the three months ended June 30, 2007, the Company recorded \$6.2 million of interest from such loans and investments. No such income had been recognized for the three months ended June 30, 2008.

Income or Losses from Equity Affiliates

The Company invests in joint ventures that are formed to acquire, develop, and/or sell real estate assets. These joint ventures are not majority owned or controlled by the Company, and are not consolidated in its financial statements. These investments are recorded under either the equity or cost method of accounting as appropriate. The Company records its share of the net income and losses from the underlying properties on a single line item in the consolidated income statements as income from equity affiliates.

Stock Based Compensation

The Company records stock-based compensation expense at the grant date fair value of the related stock-based award in accordance with SFAS No. 123R, “Accounting for Stock-Based Compensation”, (“SFAS 123R”). The Company measures the compensation costs for these shares as of the date of the grant, with subsequent remeasurement for any unvested shares granted to non-employees of the Company with such amounts expensed against earnings, at the grant date (for the portion that vest immediately) or ratably over the respective vesting periods. The cost of these grants is amortized over the vesting term using an accelerated method in accordance with Financial Accounting Standards Board (“FASB”) Interpretation No. 28 “Accounting for Stock Appreciation Rights and Other Variable Stock Options or Award Plans” (“FIN 28”), and SFAS 123R. Dividends are paid on the restricted shares as dividends are paid on shares of the Company’s common stock whether or not they are vested. Stock based compensation was disclosed in the Company’s Consolidated Income Statement under “employee compensation and benefits” for employees and under “selling and administrative” expense for non-employees.

Income Taxes

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

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

subsidiaries, the income of which are subject to federal and state income taxes. The Company did not record a provision for income taxes related to the assets that are held in taxable REIT subsidiaries for the three and six months ended June 30, 2008. The Company recorded a \$9.0 million and \$15.1 million provision for income taxes related to the assets that are held in taxable REIT subsidiaries for the three and six months ended June 30, 2007. The Company's accounting policy with respect to interest and penalties related to tax uncertainties is to classify these amounts as provision for income taxes. The Company has not recognized any interest and penalties related to tax uncertainties for the three and six months ended June 30, 2008 and 2007.

Other Comprehensive (Loss) Income

SFAS No. 130 "Reporting Comprehensive Income," divides comprehensive income into net income and other comprehensive income (loss), which includes unrealized gains and losses on available for sale securities. In addition, to the extent the Company's derivative instruments qualify as hedges under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," net unrealized gains or losses are reported as a component of accumulated other comprehensive income/(loss), see "Derivatives and Hedging Activities" below. At June 30, 2008, accumulated other comprehensive loss was \$31.0 million and consisted of \$6.6 million in unrealized losses related to available-for-sale securities and \$24.4 million of unrealized losses on derivatives designated as cash flow hedges.

Derivatives and Hedging Activities

The Company accounts for derivative financial instruments in accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"), as amended by SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities" ("SFAS 138"). SFAS 133, as amended by SFAS 138, requires an entity to recognize all derivatives as either assets or liabilities in the consolidated balance sheets and to measure those instruments at fair value. Additionally, the fair value adjustments will affect either other comprehensive income (loss) in stockholders' equity until the hedged item is recognized in earnings or net income depending on whether the derivative instrument qualifies as a hedge for accounting purposes and, if so, the nature of the hedging activity.

In the normal course of business, the Company may use a variety of derivative financial instruments to manage, or hedge, interest rate risk. These derivative financial instruments must be effective in reducing its interest rate risk exposure in order to qualify for hedge accounting. When the terms of an underlying transaction are modified, or when the underlying hedged item ceases to exist, all changes in the fair value of the instrument are marked-to-market with changes in value included in net income for each period until the derivative instrument matures or is settled. Any derivative instrument used for risk management that does not meet the hedging criteria is marked-to-market with the changes in value included in net income.

Derivatives are used for hedging purposes rather than speculation. The Company relies on quotations from a third party to determine these fair values.

Variable Interest Entities

FASB issued Interpretation No. 46R, "Consolidation of Variable Interest Entities" ("FIN 46"), which requires a variable interest entity ("VIE") to be consolidated by its primary beneficiary ("PB"). The PB is the party that absorbs a majority of the VIE's anticipated losses and/or a majority of the expected returns.

The Company has evaluated its loans and investments and investments in equity affiliates to determine whether they are VIEs. This evaluation resulted in the Company determining that its bridge loans, junior participation loans, mezzanine loans, preferred equity investments and investments in equity affiliates were potential variable interests. For each of these investments, the Company has evaluated (1) the sufficiency of the fair value of the entities' equity investments at risk to absorb losses, (2) that as a group the holders of the equity investments at risk have (a) the direct or indirect ability through voting rights to make decisions about the entities' significant activities, (b) the obligation to absorb the expected losses of the entity and their obligations are not protected directly

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

or indirectly, (c) the right to receive the expected residual return of the entity and their rights are not capped, (3) the voting rights of these investors are proportional to their obligations to absorb the expected losses of the entity, their rights to receive the expected returns of the equity, or both, and that substantially all of the entities' activities do not involve or are not conducted on behalf of an investor that has disproportionately few voting rights. As of June 30, 2008, the Company has identified 41 loans and investments which were made to entities determined to be VIEs.

Entities that issue junior subordinated notes are considered VIEs. However, it is not appropriate to consolidate these entities under the provisions of FIN 46 as equity interests are variable interests only to the extent that the investment is considered to be at risk. Since the Company's investments were funded by the entities that issued the junior subordinated notes, they are not considered to be at risk.

For the 41 VIEs identified, the Company has determined that it is not the primary beneficiaries of the VIEs and as such the VIEs should not be consolidated in the Company's financial statements. The Company's maximum exposure to loss would not exceed the carrying amount of such investments. For all other investments, the Company has determined they are not VIEs. As such, the Company has continued to account for these loans and investments as a loan or investment in equity affiliate, as appropriate.

Recently Issued Accounting Pronouncements

SFAS No. 157 — In September 2006 the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"), which defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. However, in February 2008, the FASB issued FASB Staff Position ("FSP") FAS 157-2, which delays the effective date of SFAS 157 for all non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The effective date is delayed by one year to fiscal years beginning after November 15, 2008 and interim periods within those fiscal years. Effective January 1, 2008, the Company adopted SFAS 157 for financial assets and liabilities recognized at fair value on a recurring basis. The partial adoption of SFAS 157 for financial assets and liabilities did not have an impact on the Company's Consolidated Financial Statements. The Company is currently evaluating the impact, if any, regarding the delayed application of SFAS No. 157 on the Company's Consolidated Financial Statements.

SFAS No. 159 — In February 2007 the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159") which permits entities to voluntarily choose to measure many financial instruments, and certain other items at fair value and is effective for fiscal years beginning after November 15, 2007. The Company adopted SFAS 159 as of January 1, 2008 and elected not to treat any of its financial assets or liabilities under the fair value option. The adoption of SFAS 159 did not have an impact on the Company's Consolidated Financial Statements.

FIN 39-1 — In April 2007, the FASB issued FIN No. 39-1, "Amendment of FASB Interpretation No. 39" ("FIN 39-1"). FIN 39-1 defines "right of setoff" and specifies what conditions must be met for a derivative contract to qualify for this right of setoff. FIN 39-1 also addresses the applicability of a right of setoff to derivative instruments and clarifies the circumstances in which it is appropriate to offset amounts recognized for those instruments in the balance sheet. In addition, FIN 39-1 permits offsetting of fair value amounts recognized for multiple derivative instruments executed with the same counterparty under a master netting arrangement and fair value amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) arising from the same master netting arrangement as the derivative instruments. FIN 39-1 is effective for the Company beginning January 1, 2008. The adoption of FIN 39-1 did not have a material impact on the Company's consolidated financial statements.

FSP FAS 140-3 — In February 2008, the FASB issued FASB Staff Position No. FAS 140-3 ("FSP FAS 140-3"), "Accounting for Transfers of Financial Assets and Repurchase Financing Transactions." FSP FAS 140-3 provides guidance on accounting for a transfer of a financial asset and a repurchase financing. It presumes that an

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

initial transfer of a financial asset and a repurchase financing are considered part of the same arrangement (a linked transaction) unless certain criteria are met. If the criteria are not met, the linked transaction would be recorded as a net investment, likely as a derivative, instead of recording the purchased financial asset on a gross basis along with a repurchase financing. FSP FAS 140-3 applies to reporting periods beginning after November 15, 2008 and is only applied prospectively to transactions that occur on or after the adoption date. The Company is currently evaluating the effect the adoption of FSP FAS 140-3 may have on the Company's Consolidated Financial Statements.

SOP 07-1 — In June 2007, the American Institute of Certified Public Accountants ("AICPA") issued Statement of Position ("SOP") 07-1 "Clarification of the Scope of the Audit and Accounting Guide Investment Companies and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies" ("SOP 07-1"). SOP 07-1 provides guidance for determining whether an entity is within the scope of the AICPA Audit and Accounting Guide Investment Companies. The SOP is effective for fiscal years beginning on or after December 15, 2007. However, in February 2008 the FASB issued FSP SOP 07-1-1 which delays indefinitely the effective date of SOP 07-1 and prohibits adoption of SOP 07-1 for an entity that had not adopted SOP 07-1 before issuance of the final FSP. While the Company maintains an exemption from the Investment Company Act of 1940, as amended ("Investment Company Act") and is therefore not regulated as an investment company, it is nonetheless in the process of assessing whether SOP 07-1 could be applicable upon becoming effective.

SFAS No. 141 (R) — In December 2007, the FASB issued SFAS No. 141(R), "Business Combinations" ("SFAS 141(R)") which replaces SFAS No. 141, "Business Combinations" and requires a company to recognize the assets acquired, the liabilities assumed, and any non-controlling interest in the acquired entity to be measured at their fair values as of the acquisition date. SFAS 141(R) also requires acquisition costs to be expensed as incurred and does not permit certain restructuring activities previously allowed under Emerging Issues Task Force Issue No. 95-3 to be recorded as a component of purchase accounting. SFAS 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The Company is currently evaluating the effect the adoption of SFAS 141 (R) may have on the Company's Consolidated Financial Statements.

SFAS No. 160 — In December 2007, the FASB issued SFAS No. 160 "Accounting for Non-controlling Interests in Consolidated Financial Statements — an amendment of Accounting Research Bulletin No. 51" ("SFAS 160"). SFAS 160 clarifies the classification of non-controlling interests in consolidated statements of financial position and the accounting for and reporting of transactions between the Company and holders of such non-controlling interests. Under SFAS 160, non-controlling interests are considered equity and should be reported as an element of consolidated equity. The current practice of classifying minority interests within a mezzanine section of the statement of financial position will be eliminated. Under SFAS 160, net income will encompass the total income of all consolidated subsidiaries and will require separate disclosure on the face of the income statement of income attributable to the controlling and non-controlling interests. Increases and decreases in the non-controlling ownership interest amount will be accounted for as equity transactions. When a subsidiary is deconsolidated, any retained, non-controlling equity investment in the former subsidiary and the gain or loss on the deconsolidation of the subsidiary must be measured at fair value. SFAS 160 is effective for fiscal years beginning after December 15, 2008 and earlier application is prohibited. The Company is currently evaluating the effect the adoption of SFAS 160 may have on the Company's Consolidated Financial Statements.

SFAS No. 161 — In March 2008, the FASB issued SFAS No. 161 "Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133" ("SFAS 161"). SFAS 161 requires companies with derivative instruments to disclose information that should enable financial-statement users to understand how and why a company uses derivative instruments, how derivative instruments and related hedged items are accounted for under FASB Statement No. 133 "Accounting for Derivative Instruments and Hedging Activities" and how derivative instruments and related hedged items affect a company's financial position, financial performance and cash flows. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008 and early application is permitted. Because SFAS 161 impacts the Company's disclosure and not its accounting treatment for derivative instruments and related hedged items, the Company's adoption of SFAS 161 will not impact the Company's Consolidated Financial Statements.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

SFAS No. 162 — In May 2008, the FASB issued SFAS No. 162, “The Hierarchy of Generally Accepted Accounting Principles” (“SFAS 162”). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (the GAAP hierarchy). SFAS 162 will become effective 60 days following the SEC’s approval of the Public Company Accounting Oversight Board amendments to AU Section 411, “The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles.” The Company does not currently expect the adoption of SFAS 162 to have a material effect on the Company’s Consolidated Financial Statements.

EITF 03-6-1 — In June 2008, the FASB issued FASB Staff Position EITF 03-6-1, “Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities.” This FSP addresses whether instruments granted in share-based payment transactions may be participating securities prior to vesting and, therefore, need to be included in the earnings allocation in computing basic earnings per share (“EPS”) pursuant to the two-class method described in paragraphs 60 and 61 of FASB Statement No. 128, “Earnings per Share.” A share-based payment award that contains a non-forfeitable right to receive cash when dividends are paid to common shareholders irrespective of whether that award ultimately vests or remains unvested shall be considered a participating security as these rights to dividends provide a non-contingent transfer of value to the holder of the share-based payment award. Accordingly, these awards should be included in the computation of basic EPS pursuant to the two-class method. The guidance in this FSP is effective for the Company for the fiscal year beginning January 1, 2009 and all interim periods within 2009. All prior period EPS data presented will have to be adjusted retrospectively to conform to the provisions of the FSP. Under the terms of the Company’s stock incentive plan, grantees are entitled to the right to receive dividends on the unvested portions of their restricted stock awards. There is no requirement to return these dividends in the event the unvested awards are forfeited in the future. Shares granted under the Company’s stock incentive plan are considered outstanding common shares as of the date of grant through the corresponding vesting periods, therefore, they are included in the Company’s EPS calculations. The Company does not currently expect the adoption of this FSP to have any impact on the Company’s Consolidated Financial Statements.

Note 3 — Loans and Investments

The following table sets forth the composition of the Company’s loan and investment portfolio at the dates indicated.

	June 30, 2008 (Unaudited)	Percent of Total	December 31, 2007	Percent of Total	At June 30, 2008		At December 31, 2007	
					Loan Count	Wtd. Avg. Pay Rate	Loan Count	Wtd. Avg. Pay Rate
Bridge loans	\$1,501,307,670	61%	\$1,646,505,888	63%	59	6.50%	65	7.86%
Mezzanine loans	405,781,904	16%	384,479,759	15%	42	8.35%	41	9.23%
Junior participations	318,325,595	13%	340,821,550	13%	17	6.98%	19	7.70%
Preferred equity investments	219,082,959	9%	220,387,959	9%	19	8.66%	20	9.42%
Other	15,711,549	1%	11,400,272	—	3	12.21%	2	7.99%
	<u>2,460,209,677</u>	<u>100%</u>	<u>2,603,595,428</u>	<u>100%</u>	<u>140</u>	<u>7.10%</u>	<u>147</u>	<u>8.18%</u>
Unearned revenue	(12,067,830)		(9,001,498)					
Allowance for loan losses	<u>(3,500,000)</u>		<u>(2,500,000)</u>					
Loans and investments, net	<u>\$2,444,641,847</u>		<u>\$2,592,093,930</u>					

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

The following transactions represent loans and investments that were satisfied during the six months ended June 30, 2008 in which the Company had retained a profits interest in the borrowing entity.

Richland Terrace

During 2006, the Company originated a \$7.2 million bridge loan and a \$0.3 million preferred equity investment secured by garden-style and townhouse apartments in South Carolina. The Company also had a 25.0% carried profits interest in the borrowing entity. In January 2008, the borrowing entity refinanced the property through ACM's Fannie Mae program and the Company received \$0.3 million for its profits interest as well as full repayment of the \$0.3 million preferred equity investment and the \$7.0 million outstanding balance on the bridge loan. The Company retained its 25% carried profits interest.

Lake in the Woods

At December 31, 2006, there was an \$8.5 million junior participation loan in the loan and investment portfolio that was non-performing and for which income recognition had been suspended. In March 2007, the Company purchased the senior position of the first mortgage loan associated with this property for \$34.6 million. The senior loan had a maturity date of January 2008, bore interest based at LIBOR plus 237 basis points and was also considered non-performing. During the second quarter of 2007, the Company obtained title to the property pursuant to the execution of a deed in lieu of foreclosure and subsequently sold the property to a new investor. As part of the purchase, the new investor committed approximately \$2.0 million of capital and the Company provided a total of \$45.0 million of new financing through a \$43.5 million bridge loan and a \$1.5 million preferred equity investment. The loan and investment mature in June 2012 and bear interest at a fixed rate of 7.75%. The Company also retained a 50% profits interest in the property. The Company established a \$1.0 million provision for loan loss related to this property reducing the carrying value to \$44.0 million at December 31, 2007. Interest income totaling \$0.7 million was not received or recognized on this loan during the first quarter of 2008 prior to the property being sold in February 2008 with the Company providing the financing for the new transaction as described below.

In February 2008, the property was sold for approximately \$45.9 million and the Company provided the new sponsor with a \$45.0 million first mortgage with a maturity date of February 2013 that bears interest at an initial fixed rate of 6.75% (of which 6.25% will be paid currently and 0.50% will be permitted to accumulate) which increases to 6.75% (all of which will be paid) in the second and third year and to 7.75% for the fourth and fifth year of the loan. As part of the sale, the Company assumed approximately \$2.1 million of advances for operating costs on behalf of the seller, increasing the carrying value of the loan to \$46.1 million at the time of sale. As a result of the transaction, the Company received \$0.9 million of cash proceeds, charged-off \$1.0 million against the allowance for loan losses and incurred an additional loss of \$0.2 million which was recorded in selling and administrative expenses.

The new sponsor funded \$3.9 million of equity including a \$2.6 million cash interest and capital expenditure reserve and \$1.3 million of closing costs. In accordance with the terms of the new agreement, the Company has not retained a profits interest in the property.

The following transactions represent loans and investments originated by the Company during the six months ended June 30, 2008 in which the Company retained a profits interest in the borrowing entity.

Windrush Village

At March 31, 2008, the Company had a \$13.8 million bridge loan secured by a 210 unit multi-family property located in Tallahassee, Florida that was scheduled to mature in June 2008 and bore interest at LIBOR plus 2.50% with a LIBOR floor of 3.50%. The Company established a \$1.5 million provision for loan loss related to this property during the fourth quarter of 2007, reducing the carrying value to \$12.3 million at March 31, 2008. In May 2008, the Company received \$0.3 million from the borrower plus a \$0.3 million note from the borrower payable in 16 monthly installments, reducing the carrying amount to \$11.7 million. In May 2008, the property was sold for approximately \$11.8 million and the Company provided the purchaser with a \$12.8 million loan and investment, of

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

which approximately \$11.3 million was funded as of June 30, 2008, with a fixed interest rate of 6.22% and a maturity date in May 2011. The Company also received a 25% equity participation interest in the property. As a result of this transaction, the Company recorded a loss of approximately \$1.7 million, of which \$1.5 million was charged—off against the allowance for loan losses and approximately \$0.2 million was recorded in selling and administrative expenses in the second quarter of 2008.

Concentration of Borrower Risk

The Company is subject to concentration risk in that, as of June 30, 2008, the unpaid principal balance related to 31 loans with five unrelated borrowers represented approximately 24% of total assets. The Company had 140 loans and investments as of June 30, 2008. As of June 30, 2008, 40.5%, 11.5%, and 11.4% of the outstanding balance of the Company's loans and investments portfolio had underlying properties in New York, Florida and California, respectively.

Impaired Loans and Allowance for Loan Losses

The Company considers a loan impaired when, based upon current information and events, it is probable that it will be unable to collect all amounts due for both principal and interest according to the contractual terms of the loan agreement. As a result of the Company's normal quarterly loan review at June 30, 2008, it was determined that three loans with an aggregate outstanding principal balance of \$75.2 million were impaired. At December 31, 2007, two multi-family loans with an aggregate outstanding principal balance of \$58.5 million were impaired.

The Company performed an evaluation of the loans and determined that the fair value of the underlying collateral securing the impaired loans was less than the net carrying value of the loans, resulting in the Company recording a \$2.0 million and \$5.0 million provision for loan losses for the three and six months ended June 30, 2008, respectively. The Company did not record a provision for loan losses for the three and six months ended June 30, 2007.

During the fourth quarter of 2007, the Company established a \$1.0 million loan loss reserve related to a \$45.0 million loan and investment on the Lake in the Woods property. In the first quarter of 2008, the property was sold and as a result of the transaction, the Company charged-off \$1.0 million against the allowance for loan losses and incurred an additional loss of \$0.2 million, which was recorded in selling and administrative expenses. See the Lake in the Woods discussion above for further details on the transaction.

During the fourth quarter of 2007, the Company established a \$1.5 million loan loss reserve related to a \$13.8 million bridge loan on Windrush Village property. In the second quarter of 2008, the property was sold and as a result of the transaction, the Company charged-off \$1.5 million against the allowance for loan losses and incurred an additional loss of \$0.2 million, which was recorded in selling and administrative expenses related to additional expenses incurred. See the Windrush Village discussion above for further details on the transaction.

At December 31, 2007, the Company had a \$5.0 million mezzanine loan secured by an office building located in Indianapolis, Indiana that was scheduled to mature in June 2012 and bore interest at a fixed rate of 10.72%. During the first quarter, the Company established a \$1.5 million provision for loan loss related to this property reducing the carrying value to \$3.5 million at March 31, 2008. In April 2008, the Company was the winning bidder at a UCC foreclosure sale of the entity which owns the equity interest in the property securing this loan and a \$41.4 million first mortgage on the property. As a result, during the second quarter, the Company recorded this investment on its balance sheet as real estate owned at fair value which included the Company's \$3.5 million carrying value of the loan, recorded the \$41.4 million first lien in mortgage notes payable and recorded a net loss for the period of approximately \$19,000 which was recorded in selling and administrative expenses.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

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

	For the Six Months Ended June 30, 2008
Allowance at beginning of the period	\$ 2,500,000
Provision for loan losses	5,000,000
Charge-offs	(2,500,000)
Reclassified to real estate owned, net	(1,500,000)
Allowance at end of the period	<u>\$ 3,500,000</u>

As of June 30, 2008, two loans with an outstanding principal balance of approximately \$80.1 million were classified as non-performing. Income is recognized on a cash basis only to the extent it is received. Full income recognition will resume when the loan becomes contractually current and performance has recommenced. At December 31, 2007, there were no non-performing loans.

The Company has a \$70.4 million bridge loan on a land development project in New York City located at 303 East 51st Street. This loan had an initial maturity date of May 2008 with one six month extension option and an interest rate of Libor plus 4.25% with a Libor floor of 5.32%. On March 15, 2008, there was a tragic construction accident related to the development of this project and a stop work order has been issued by the city for an undeterminable amount of time. As a result, effective April 1, 2008, the Company will not record interest income on this loan until it is received. The property did not sustain significant damage. On May 1, 2008, the Company entered into agreements with the borrower, pursuant to which the Company received a \$0.5 million cash payment which was applied to interest and agreed to defer mortgage payments until July 1, 2008. In addition, the borrower acknowledged the Company's right to directly receive and apply insurance proceeds as they may be received. During the second quarter the Company received \$0.1 million in insurance proceeds which was recorded as interest income. In July 2008, the Company elected to begin the foreclosure process on the entity that owns the property. The principal amount of this loan is not deemed to be impaired at this time and no loan loss reserve has been recorded to date.

In addition, as of June 30, 2008, one of the three loans reserved for, with an outstanding principal balance of approximately \$9.9 million, had been classified as non-performing.

Note 4 — Available-For-Sale Securities

The following is a summary of the Company's available-for-sale securities at June 30, 2008.

	<u>Amortized Cost</u>	<u>Unrealized Loss</u>	<u>Estimated Fair Value</u>
Common equity securities	<u>\$16,715,584</u>	<u>\$(6,603,825)</u>	<u>\$10,111,759</u>
Total available-for-sale securities	<u>\$16,715,584</u>	<u>\$(6,603,825)</u>	<u>\$10,111,759</u>

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

The following is a summary of the Company's available-for-sale securities at December 31, 2007.

	<u>Amortized Cost</u>	<u>Unrealized Loss</u>	<u>Estimated Fair Value</u>
Common equity securities	\$ 16,715,584	\$(1,018,841)	\$15,696,743
Total available-for-sale securities	<u>\$ 16,715,584</u>	<u>\$(1,018,841)</u>	<u>\$15,696,743</u>

During 2007, the Company purchased 2,939,465 shares of common stock of CBRE Realty Finance, Inc., a commercial real estate specialty finance company, which had a fair value of \$10.1 million, at June 30, 2008 and a fair value of \$15.7 million at December 31, 2007. As of June 30, 2008, these securities have been in an unrealized loss position for less than twelve months and the Company does not consider these investments to be other-than-temporarily impaired. The Company has a margin loan agreement with a financial institution related to the purchases of this security. The margin loan may not exceed \$7.0 million, bears interest at pricing over LIBOR, and is due upon demand from the lender. The balance of the margin loan agreement was approximately \$1.7 million at June 30, 2008. In July 2008, the margin loan has subsequently been repaid in full.

The cumulative amount of other comprehensive loss related to unrealized losses on these securities as of June 30, 2008 and December 31, 2007 was \$6.6 million and \$1.0 million, respectively.

Note 5 — Securities Held-to-Maturity

The following is a summary of the Company's securities held-to-maturity at June 30, 2008.

	<u>Face Value</u>	<u>Amortized Cost</u>	<u>Unrealized Gain</u>	<u>Unrealized Loss</u>	<u>Estimated Fair Value</u>
Collateralized debt obligation bonds	\$82,700,000	\$58,498,406	\$338,290	\$(559,216)	\$58,277,480
Total securities held-to-maturity	<u>\$82,700,000</u>	<u>\$58,498,406</u>	<u>\$338,290</u>	<u>\$(559,216)</u>	<u>\$58,277,480</u>

The following is a summary of the underlying credit rating of the Company's securities held-to-maturity at June 30, 2008.

<u>Rating</u>	<u>Amortized Cost</u>	<u>Percent of Total</u>
AAA	\$ 47,941,367	82%
AA	9,145,329	16%
BBB	1,411,710	2%
	<u>\$ 58,498,406</u>	<u>100%</u>

During the second quarter of 2008, the Company purchased \$82.7 million of investment grade CRE collateralized debt obligation bonds for \$58.1 million. The \$24.6 million discount will be accreted into interest income on an effective yield adjusted for actual prepayment activity over the average life of the related security as a yield adjustment. For the three months ended June 30, 2008, the Company accreted approximately \$0.4 million of this discount into interest income. These securities bear interest at a weighted average spread of 40 basis points over Libor and have a weighted average stated maturity of 38.2 years. At June 30, 2008, the average yield on these securities based on their face values was 7.52%, including the accretion of discount. The Company did not have any securities held-to-maturity at December 31, 2007.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

Securities held to maturity are carried at cost, net of unamortized premiums and discounts, which are recognized in interest income using an effective yield or “interest” method. Decreases in fair value deemed to be other than temporary would be reported as a loss on the Company’s financial statements.

In addition, during the second quarter, the Company entered into a repurchase agreement with a financial institution for the purpose of financing five of the CDO bond securities with a face value of \$75.0 million. At June 30, 2008, current borrowings totaled approximately \$40.2 million, or 54% of the face value of the securities.

Note 6 — Investment in Equity Affiliates

The following is a summary of the Company’s investment in equity affiliates at June 30, 2008 and December 31, 2007:

Equity Affiliates	Investment in Equity Affiliates at		Outstanding Loan
	June 30, 2008	December 31, 2007	Balance to Equity Affiliates at June 30, 2008
930 Flushing & 80 Evergreen	\$ 523,225	\$ 700,724	\$ 24,789,094
450 West 33 rd Street	1,136,960	1,136,960	50,000,000
1107 Broadway	5,720,000	5,720,000	—
1133 York Ave	7,693	7,693	—
Alpine Meadows	12,657,813	13,219,813	30,500,000
St. John’s Development	500,000	500,000	25,000,000
Issuance of Junior Subordinated Notes	8,305,000	8,305,000	—
Total	<u>\$ 28,850,691</u>	<u>\$ 29,590,190</u>	<u>\$ 130,289,094</u>

930 Flushing & 80 Evergreen

During the six months ended June 30, 2008, the Company recorded \$0.2 million as a return of capital from its equity investment on a capital contribution made in 2007. In addition, during the second quarter of 2008, \$4.8 million was received by the Company for the repayment in full of a bridge loan on the 80 Evergreen property from refinance proceeds of the borrower.

450 West 33rd Street

In May 2007, the Company, as part of an investor group for the 450 West 33rd Street partnership, transferred control of the underlying property (an office building) to Broadway Partners for a value of approximately \$664.0 million. The investor group, on a pro-rata basis, retained an approximate 2% ownership interest in the property and 50% of the property’s air rights which resulted in the Company retaining an investment in equity affiliates of approximately \$1.1 million related to its 29% interest in the 2% retained ownership. In accordance with this transaction, the joint venture members agreed to guarantee \$258.1 million of the \$517.0 million of new debt outstanding on the property. The guarantee expires at the earlier of maturity or prepayment of the debt and was allocated to the members in accordance with their ownership percentages. The guarantee is callable, on a pro-rata basis, if the market value of the property declines below the \$258.1 million of debt guaranteed. The Company’s portion of the guarantee is \$76.3 million. The transaction was structured to provide for a tax deferral for an

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

estimated period of seven years. The Company recorded deferred revenue of approximately \$77.1 million as a result of the guarantee on a portion of the new debt.

Prime Outlets

In December 2003, the Company invested approximately \$2.1 million in exchange for a 50% non-controlling interest in Prime Outlets Member, LLC ("POM"), which owns 15% of a real estate holding company that owns and operates a portfolio of factory outlet shopping centers. The Company accounts for this investment under the equity method. Additionally, the Company owns a 16.67% carried profits interest through a consolidated entity which has a 25% interest in POM with a third party member owning the remaining 8.33%.

In June 2008, the Company entered into an agreement to transfer its 16.67% interest in POM, at a value of approximately \$37 million, in exchange for preferred and common operating partnership units of Lightstone Value Plus REIT L.P.

In connection with this agreement, the Company borrowed from Lightstone Value Plus Real Estate Investment Trust, Inc. approximately \$33 million, which is initially secured by its 16.67% interest in POM, has an eight year term, and bears interest at a fixed rate of 4% with payment of the interest deferred until the closing of the transaction. Upon the closing of this transaction, which is expected to occur on or before June 26, 2009, the Company will exchange its 16.67% interest in Prime Outlets for approximately \$37 million of preferred and common operating partnership units in Lightstone Value Plus REIT L.P. The \$33 million loan will then be secured by the Company's preferred and common operating partnership units. The preferred units will pay a preferred return at a fixed rate of 4.63% and after five years, they may be redeemed by Lightstone Value Plus REIT L.P. for cash at par and the loan would become due upon such redemption. The transaction provides for a tax deferral for an estimated period of five years, subject to certain carve out provisions. In addition, the Company will pay an incentive management fee to its manager of approximately \$7.3 million.

During the second quarter of 2008, the Company recorded approximately \$33.0 million of cash, \$49.5 million of debt related to the proceeds received from the loan secured by the entity's 25% interest in POM which was recorded in notes payable, a \$16.5 million receivable from the third party member which was recorded in other assets and a deferred expense related to the incentive management fee of approximately \$7.3 million. Upon closing this transaction, which is expected to occur on or before June 26, 2009, the Company estimates that it will record an investment of approximately \$55 million for the preferred and common operating partnership units, income of approximately \$49 million, minority interest expense of approximately \$16 million related to the third party members portion of income recorded, management fee expense of approximately \$7.3 million, a deferred gain of approximately \$5 million and minority interest due to the third party member of approximately \$18 million.

Alpine Meadows

In July 2007, the Company invested \$13.2 million in exchange for a 39% profits interest with an 18% preferred return in the Alpine Meadows ski resort, which consists of approximately 2,163 total acres in northwestern Lake Tahoe, California. The Company's invested capital represents 65% of the total equity of the transaction and the Company will be allocated 65% of the losses. The Company also provided a \$30.5 million first mortgage loan that matures in August 2009 and bears interest at pricing over one month LIBOR. The outstanding balance on this loan was \$30.5 million at June 30, 2008. During the second quarter of 2008, the Company recorded a \$0.6 million loss from this equity investment. This amount reflects Arbor's portion of the joint venture's losses, including depreciation expense, and was recorded in loss from equity affiliates and as a reduction to the Company's investment in equity affiliates on the balance sheet.

Note 7 — Debt Obligations

The Company utilizes repurchase agreements, term and revolving credit agreements, warehouse lines of credit, working capital lines, loan participations, collateralized debt obligations and junior subordinated notes to

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

finance certain of its loans and investments. Borrowings underlying these arrangements are primarily secured by a significant amount of the Company's loans and investments.

Repurchase Agreements

The following table outlines borrowings under the Company's repurchase agreements as of June 30, 2008 and December 31, 2007:

	<u>June 30, 2008</u>		<u>December 31, 2007</u>	
	<u>Debt Carrying Value</u>	<u>Collateral Carrying Value</u>	<u>Debt Carrying Value</u>	<u>Collateral Carrying Value</u>
Repurchase agreement, Nomura Credit and Capital, Inc., \$100 million committed line, expired December 2007 with final repayment due June 2008 (repaid in February 2008), interest is variable based on one-month LIBOR; the weighted average note rate was 0% and 7.10%, respectively	\$ —	\$ —	\$ 23,321,740	\$ 38,000,000
Repurchase agreement, financial institution, \$200 million committed line, expiration October 2009, interest is variable based on one-month LIBOR, the weighted average note rate was 3.54% and 6.03%, respectively	115,209,819	135,927,679	165,571,254	241,547,947
Repurchase agreement, financial institution, \$100 million committed line, expiration September 2008, interest is variable based on one-month LIBOR; the weighted average note rate was 4.49% and 6.66%, respectively	43,383,318	54,385,478	56,044,935	70,103,865
Repurchase agreement, financial institution, an uncommitted line, expiration May 2010, interest is variable based on one and three month LIBOR; the weighted average note rate was 4.09%	<u>40,162,500</u>	<u>75,000,000</u>	<u>—</u>	<u>—</u>
Total repurchase agreements	<u>\$ 198,755,637</u>	<u>\$ 265,313,157</u>	<u>\$ 244,937,929</u>	<u>\$ 349,651,812</u>

The Company's \$100.0 million master repurchase agreement with Nomura Credit and Capital, Inc. expired in December 2007. The Company exercised its right under the repurchase agreement to extend the repayment date until June 2008. This facility was repaid in its entirety in February 2008.

The Company has a \$100.0 million repurchase agreement that bears interest at pricing over LIBOR and has a maturity date of September 2008. In January 2008, the Company was notified that no further advances could be taken under this facility. The facility matures in September 2008 and, under the terms of the repurchase agreement, the facility will be paid in its entirety by December 2008.

In April 2008, the Company entered into an uncommitted master repurchase agreement with a financial institution for the purpose of financing its CRE CDO bond securities. The facility has a two year term from the effective date of the agreement and bears interest at pricing over LIBOR. At June 30, 2008, the aggregate outstanding balance in this facility was approximately \$40.2 million.

In certain circumstances, the Company has financed the purchase of investments from a counterparty through a repurchase agreement with that same counterparty. The Company currently records these investments in the same manner as other investments financed with repurchase agreements, with the investment recorded as an asset and the related borrowing under the repurchase agreement as a liability on the Company's consolidated balance sheet. Interest income earned on the investments and interest expense incurred on the repurchase obligations are reported separately on the consolidated income statement. These transactions may not qualify as a purchase by the Company under FSP FAS 140-3 which is effective for fiscal years beginning after November 15, 2008. The Company would be required to present the net investment on the balance sheet as a derivative with the corresponding change in fair value of the derivative being recorded in the income statement. The value of the

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

derivative would reflect not only changes in the value of the underlying investment, but also changes in the value of the underlying credit provided by the counterparty. See Note 2 —“Summary of Significant Accounting Policies — Recently Issued Accounting Pronouncements” for further details.

Junior Subordinated Notes

The following table outlines borrowings under the Company’s junior subordinated notes as of June 30, 2008 and December 31, 2007:

	<u>June 30, 2008</u>	<u>December 31, 2007</u>
	<u>Debt</u> <u>Carrying</u> <u>Value</u>	<u>Debt</u> <u>Carrying</u> <u>Value</u>
Junior subordinated notes, maturity March 2034, unsecured, face amount of \$27.1 million, interest rate variable based on three-month LIBOR, the weighted average note rate was 6.53% and 8.58%, respectively	\$ 27,070,000	\$ 27,070,000
Junior subordinated notes, maturity March 2034, unsecured, face amount of \$25.8 million, interest rate variable based on three-month LIBOR, the weighted average note rate was 8.24% and 8.31%, respectively	25,780,000	25,780,000
Junior subordinated notes, maturity April 2035, unsecured, face amount of \$25.8 million, interest rate variable based on three-month LIBOR, the weighted average note rate was 7.36% and 7.42%, respectively	25,774,000	25,774,000
Junior subordinated notes, maturity July 2035, unsecured, face amount of \$25.8 million, interest rate variable based on three-month LIBOR, the weighted average note rate was 6.64% and 8.23%, respectively	25,774,000	25,774,000
Junior subordinated notes, maturity January 2036, unsecured, face amount of \$51.6 million, interest rate variable based on three-month LIBOR, the weighted average note rate was 7.01% and 7.76%, respectively	51,550,000	51,550,000
Junior subordinated notes, maturity July 2036, unsecured, face amount of \$51.6 million, interest rate variable based on three-month LIBOR, the weighted average note rate was 7.87% and 7.93%, respectively	51,550,000	51,550,000
Junior subordinated notes, maturity June 2036, unsecured, face amount of \$15.5 million, interest rate variable based on three-month LIBOR, the weighted average note rate was 7.79% and 7.85%, respectively	15,464,000	15,464,000
Junior subordinated notes, maturity April 2037, unsecured, face amount of \$14.4 million, interest rate variable based on three-month LIBOR, the weighted average note rate was 7.17% and 7.24%, respectively	14,433,000	14,433,000
Junior subordinated notes, maturity April 2037, unsecured, face amount of \$38.7 million, interest rate variable based on three-month LIBOR, the weighted average note rate was 7.17% and 7.23%, respectively	<u>38,660,000</u>	<u>38,660,000</u>
Total junior subordinated notes	<u>\$ 276,055,000</u>	<u>\$ 276,055,000</u>

The junior subordinated notes are unsecured, have a maturity of 30 years, pay interest quarterly at a floating rate of interest based on three-month LIBOR and, absent the occurrence of special events, are not redeemable during the first five years.

The outstanding balance under these facilities was \$276.1 million at both June 30, 2008 and December 31, 2007. The current weighted average note rate was 7.41% at June 30, 2008 and 7.84% December 31, 2007. The impact of these entities in accordance with FIN 46R “Consolidation of Variable Interest Entities” is discussed in Note 2.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

Notes Payable

The following table outlines borrowings under the Company’s notes payable as of June 30, 2008 and December 31, 2007:

	<u>June 30, 2008</u>		<u>December 31, 2007</u>	
	<u>Debt Carrying Value</u>	<u>Collateral Carrying Value</u>	<u>Debt Carrying Value</u>	<u>Collateral Carrying Value</u>
Term credit agreement, Wachovia Bank, National Association, \$473 million committed line, expiration November 2009, interest is variable based on one-month LIBOR; the weighted average note rate was 4.99% and 6.87%, respectively	\$362,494,111	\$525,517,637	\$412,095,278	\$ 768,814,515
Revolving credit agreement, Wachovia Bank, National Association, \$100 million committed line, expiration November 2009, interest is variable based on one-month LIBOR; the weighted average note rate was 5.14% and 6.89%, respectively	65,267,133	99,005,797	6,759,220	26,127,598
Term credit agreement, Wachovia Bank, National Association, \$69 million committed line, expiration November 2009, interest is variable based on one-month LIBOR; the weighted average note rate was 5.03% and 7.36%, respectively	53,211,348	115,000,000	66,500,000	115,000,000
Bridge loan warehouse, financial institution, \$90 million committed line, expiration October 2008, interest rate variable based on Prime or LIBOR, the weighted average note rate was 5.27% and 6.51%, respectively	55,707,875	71,586,209	62,897,875	93,050,000
Working capital facility, Wachovia Bank, National Association; \$60 million committed line, expiration June 2009 with two one year renewal options, interest is variable based on one-month LIBOR, the weighted average note rate was 7.57% and 6.96%, respectively	47,907,965	—	47,907,965	—
Note payable from investment in equity affiliates, \$49.5 million, expiration July 2016, interest is fixed, the weighted average note rate was 4.00%	49,500,000	—	—	—
Junior loan participation, maturity May 2010, secured by the Company’s interest in a first mortgage loan with a principal balance of \$1.3 million, participation interest was based on a portion of the interest received from the loan which has a fixed rate of interest	1,300,000	—	—	—
Total notes payable	<u>\$635,388,432</u>	<u>\$811,109,643</u>	<u>\$596,160,338</u>	<u>\$1,002,992,113</u>

The Company has a \$60.0 million working capital facility with Wachovia Bank, National Association (“Wachovia”) that had an expiration date of June 2008. In July 2008, the facility was extended for one year to June 2009 and was amended to a \$45 million facility. In addition, the amendment includes required quarterly paydowns of \$3.0 million beginning October 1, 2008 and an interest rate increase from 210 basis points over Libor to a rate of 500 basis points over Libor. At June 30, 2008, the aggregate outstanding balance under this facility was \$47.9 million.

The Company has a \$90 million bridge loan warehouse agreement with a maturity of October 2008. The Company currently expects to renew this facility for one year. At June 30, 2008, the aggregate outstanding balance under this facility was \$55.7 million.

During the second quarter of 2008, the Company recorded a \$49.5 million note payable related to the POM equity kicker transaction. The note is initially secured by the Company’s 16.67% interest in POM, matures in July 2016 and bears interest at a fixed rate of 4% with payment deferred until the closing of the transaction. See Note 6 — “Investment in Equity Affiliates” for further details.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

We have one junior loan participation with a total outstanding balance at June 30, 2008 of \$1.3 million. This participation borrowing has a maturity date equal to the corresponding mortgage loan and is secured by the participant's interest in the mortgage loan. Interest expense is based on a portion of the interest received from the loan.

In November 2007, the Company entered in two new credit agreements with Wachovia which replaced two of the Company's existing repurchase agreements totaling \$757.0 million with Wachovia and an affiliate of Wachovia.

The first credit agreement consists of a \$473.0 million term loan and a \$100.0 million revolving commitment. The facility has a commitment period of two years with a one year extension option to November 2010, bears interest at pricing over LIBOR, and has eliminated the mark to market risk as it relates to interest rate spreads that existed under the terms of the repurchase agreements. The advance rates for this term facility are similar to the advance rates that existed under the previous repurchase agreements. The \$473.0 million term loan component has repayment provisions which include reducing the outstanding balance to \$300.0 million by December 31, 2008. The outstanding balance under the term component of this facility was \$362.5 million at June 30, 2008. In July 2008, the Company paid down an additional \$43.4 million decreasing the outstanding balance to \$319.1 million at July 31, 2008. The \$100.0 million revolving commitment is used to finance new investments and can be increased to \$200.0 million when the term loan is paid down to \$400.0 million. The term loan was paid down to \$400.0 million on February 15, 2008. The outstanding balance under the revolving component of this facility was \$65.3 million at June 30, 2008.

The second credit agreement is a \$69.0 million term loan which has a commitment period of two years with a one year extension option to November 2010 and bears interest at pricing over LIBOR. This agreement includes \$10.0 million of annual repayment provisions in quarterly installments. The advance rate on this term facility is higher than the advance rate for the collateral that was in the repurchase agreement and the facility eliminates the mark to market risk as it relates to interest rate spreads that existed under the terms of the repurchase agreement. The Company has also pledged its 24% equity interest in POM as part of this agreement. In the second and third year of this term facility, the Company is required to paydown this facility by an additional amount equal to distributions in excess of \$10.0 million per year received by the Company from its investment in POM, if any. In connection with the POM transaction in July 2008, the Company agreed to pay down approximately \$11.6 million of this facility from proceeds received from this transaction, decreasing the outstanding balance to \$41.6 million at July 31, 2008. In addition, 16.7% of the Company's 24.2% equity interest in POM was released as collateral in conjunction with this paydown. See Note 6 — "Investment in Equity Affiliates" for further details. The outstanding balance under the term component of this facility was \$53.2 million at June 30, 2008.

In addition, during the second quarter of 2008, the Company recorded a \$41.4 million first lien mortgage related to the foreclosure of an entity in which the Company had a \$5.0 million mezzanine loan. The mortgage bears interest at a fixed rate and was recorded in mortgage note payable. See Note 3 — "Loans and Investments" for further details.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

Collateralized Debt Obligations

The following table outlines borrowings under the Company's collateralized debt obligations as of June 30, 2008 and December 31, 2007:

	<u>June 30, 2008</u> Debt Carrying Value	<u>December 31, 2007</u> Debt Carrying Value
CDO I — Issued four investment grade tranches January 19, 2005. Reinvestment period through April 2009. Interest rate variable based on three-month LIBOR; the weighted average note rate was 4.55% and 5.48%, respectively	\$ 279,319,000	\$ 283,319,000
CDO II — Issued nine investment grade tranches January 11, 2006. Reinvestment period through April 2011. Interest is variable based on three-month LIBOR; the weighted average note rate was 4.56% and 5.58%, respectively	345,630,000	347,990,000
CDO III — Issued 10 investment grade tranches December 14, 2006. Reinvestment period through January 2012. Interest is variable based on three-month LIBOR; the weighted average note rate was 3.69% and 5.12%, respectively	504,700,000	519,700,000
Total CDOs .	<u>\$ 1,129,649,000</u>	<u>\$ 1,151,009,000</u>

Proceeds from CDO I and CDO II are distributed quarterly with approximately \$2.0 million and \$1.2 million, respectively, being paid to investors as a reduction of the CDO liability.

CDO III has \$100.0 million revolving note class that provides a revolving note facility. The outstanding note balance for CDO III was \$504.7 million at June 30, 2008 which included \$57.2 million outstanding under the revolving note facility. The outstanding note balance for CDO III was \$519.7 million at December 31, 2007 which included \$72.2 million outstanding under the revolving note facility.

The Company intends to own these portfolios of real estate-related assets until their maturities and accounts for these transactions on its balance sheet as financing facilities. For accounting purposes, CDOs are consolidated in the Company's financial statements. The investment grade tranches are treated as secured financings, and are non-recourse to the Company.

Debt Covenants

Each of the credit facilities contains various financial covenants and restrictions, including fixed and senior fixed charge coverage ratios. The Company was in compliance with all financial covenants and restrictions for the periods presented with the exception of the fixed and senior fixed charge coverage ratio for one financial institution for the three months ended June 30, 2008. The Company is required to have a fixed charge coverage ratio of 1.50 to 1.0 and a senior fixed charge coverage ratio of 1.75 to 1.0, the Company's ratio was 1.49 to 1.0 and 1.72 to 1.0, respectively, at the end of the second quarter. The Company has obtained waivers of these covenants for June 30, 2008 from this financial institution and expects to permanently amend these covenant calculations.

Note 8 — Minority Interest

On July 1, 2003, ACM contributed \$213.1 million of structured finance assets and \$169.2 million of borrowings supported by \$43.9 million of equity in exchange for a commensurate equity ownership in ARLP, the

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

Company's operating partnership. This transaction was accounted for as minority interest in ARLP. In April 2004, the Company issued 6,750,000 shares of its common stock in an initial public offering and a concurrent offering to one of the Company's directors. In May 2004, the underwriters of the initial public offering exercised a portion of their over-allotment option, which resulted in the issuance of 524,200 additional shares.

At December 31, 2007, minority interest was \$72.9 million reflecting ACM's 15.5% limited partnership interest in ARLP. In June 2008, ACM exercised its right to redeem its 3,776,069 operating partnership units ("OP units") in the Company's operating partnership for shares of the Company's common stock on a one-for-one basis. As a result, ACM's operating partnership ownership interest in the Company and the balance of minority interest were reduced to zero as of June 30, 2008. In accordance with EITF 95-7, "Implementation Issues Related to the Treatment of Minority Interests in Certain Real Estate Investment Trusts," the redemption of the minority interest in exchange for the Company's common stock was recorded at book value and recorded directly to equity in additional paid-in capital. In addition, the special voting preferred shares paired with each OP unit, pursuant to a pairing agreement, were redeemed simultaneously and cancelled by the Company. In connection with this transaction, the Company's Board of Directors approved a resolution of the Company's charter allowing ACM and Ivan Kaufman to own more than the 7% ownership limitation of the Company's outstanding common stock.

Note 9 — Derivative Financial Instruments

The Company accounts for derivative financial instruments in accordance with SFAS No. 133 which requires an entity to recognize all derivatives as either assets or liabilities in the consolidated balance sheets and to measure those instruments at fair value. Additionally, the fair value adjustments will affect either other comprehensive income in stockholders' equity until the hedged item is recognized in earnings or net income, depending on whether the derivative instrument qualifies as a hedge for accounting purposes and, if so, the nature of the hedging activity.

In connection with the Company's interest rate risk management, the Company periodically hedges a portion of its interest rate risk by entering into derivative financial instrument contracts. The Company has entered into various interest rate swap agreements to hedge its exposure to interest rate risk on (i) variable rate borrowings as it relates to fixed rate loans; (ii) the difference between the CDO investor return being based on the three-month LIBOR index while the supporting assets of the CDO are based on the one-month LIBOR index; and (iii) the issuance of variable rate junior subordinated notes.

Derivative financial instruments must be effective in reducing the Company's interest rate risk exposure in order to qualify for hedge accounting. When the terms of an underlying transaction are modified, or when the underlying hedged item ceases to exist, all changes in the fair value of the instrument are marked-to-market with changes in value included in net income for each period until the derivative instrument matures or is settled. Any derivative instrument used for risk management that does not meet the hedging criteria is marked-to-market with the changes in value included in net income.

The following is a summary of the derivative financial instruments held by the Company as of June 30, 2008 and December 31, 2007: (Dollars in Thousands)

Designation\ Cash Flow	Notional Value		Expiration Date	Fair Value	
	June 30, 2008	December 31, 2007		June 30, 2008	December 31, 2007
Non-Qualifying	\$ 1,303,631	\$ 1,303,631	2009 — 2015	\$ 3,218	\$ 2,543
Qualifying	\$ 899,173	\$ 776,232	2008 — 2017	\$ (26,121)	\$ (29,872)

The fair value of Non-Qualifying Hedges was \$3.2 million and \$2.5 million as of June 30, 2008 and December 31, 2007, respectively, and is recorded in other assets in the Consolidated Balance Sheet. For the six

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

months ended June 30, 2008 and 2007, the change in fair value of the Non-Qualifying Swaps was \$0.7 million and (\$0.5) million, respectively and is recorded in interest expense on the Consolidated Income Statement.

The fair value of Qualifying Cash Flow Hedges as of June 30, 2008 and December 31, 2007 was \$(26.1) million and \$(29.9) million, respectively, and was recorded in other comprehensive loss and in other liabilities in the Consolidated Balance Sheet. As of June 30, 2008, the Company expects to reclassify approximately \$(4.6) million of other comprehensive loss from Qualifying Cash Flow Hedges to interest expense over the next twelve months assuming interest rates on that date are held constant.

Gains and losses on terminated swaps are being accreted to income over the original life of the hedging instruments as the hedged item was designated as current and future outstanding LIBOR based debt, which has an indeterminate life, and the hedged transaction is still more likely than not to occur. The Company has deferred approximately \$1.7 million and \$1.9 million of such gains through other comprehensive income at June 30, 2008 and December 31, 2007, respectively. The Company recorded \$0.2 million as a reduction to interest expense related to the accretion of these gains for both the six months ended June 30, 2008 and 2007. The Company expects to accrete approximately \$0.3 million of this deferred income to earnings over the next twelve months.

The cumulative amount of other comprehensive loss related to net unrealized losses on derivatives designated as Cash Flow Hedges as of June 30, 2008 and December 31, 2007 of \$(24.4) million and \$(28.0) million, respectively, is a combination of the fair value of qualifying cash flow hedges of \$(26.1) million and \$(29.9) million, respectively, and deferred gains on termination of interest swaps of \$1.7 million and \$1.9 million, respectively. The remaining portion included in other comprehensive loss is related to the Company's available-for-sale securities as discussed in Note 4 "Available-For-Sale Securities" of these Consolidated Financial Statements.

Note 10 — Fair Value Measurements

The Company adopted SFAS No. 157, "Fair Value Measurements" for financial assets and liabilities effective January 1, 2008. This standard defines fair value, provides guidance for measuring fair value and requires certain disclosures. This standard does not require any new fair value measurements, but rather applies to all other accounting pronouncements that require or permit fair value measurements.

Fair value is defined as the price at which an asset could be exchanged in a current transaction between knowledgeable, willing parties. A liability's fair value is defined as the amount that would be paid to transfer the liability to a new obligor, not the amount that would be paid to settle the liability with the creditor. Where available, fair value is based on observable market prices or parameters or derived from such prices or parameters. Where observable prices or inputs are not available, valuation models are applied. These valuation techniques involve some level of management estimation and judgment, the degree of which is dependent on the price transparency for the instruments or market and the instruments' complexity.

Assets and liabilities disclosed at fair value are categorized based upon the level of judgment associated with the inputs used to measure their fair value. Hierarchical levels, defined by SFAS 157 and directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets and liabilities, are as follows:

- Level 1 — Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date. The types of assets and liabilities carried at Level 1 fair value generally are government and agency securities, equities listed in active markets, investments in publicly traded mutual funds with quoted market prices and listed derivatives.
- Level 2 — Inputs (other than quoted prices included in Level 1) are either directly or indirectly observable for the asset or liability through correlation with market data at the measurement date and for the duration of the instrument's anticipated life. Fair valued assets and liabilities that are generally included in this category are non-government securities, municipal bonds, certain hybrid financial instruments, certain mortgage and asset backed securities, certain corporate debt, certain commitments and guarantees, certain private equity investments and certain derivatives.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

- Level 3 — Inputs reflect management’s best estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model. Generally, assets and liabilities carried at fair value and included in this category are certain mortgage and asset-backed securities, certain corporate debt, certain private equity investments, certain municipal bonds, certain commitments and guarantees and certain derivatives.

Determining which category as asset or liability falls within the hierarchy requires significant judgment and the Company evaluates its hierarchy disclosures each quarter.

The Company measures certain financial assets and financial liabilities at fair value on a recurring basis, including available—for—sale securities and derivative financial instruments. The fair value of these financial assets and liabilities was determined using the following inputs as of June 30, 2008.

	Carrying Value	Fair Value	Fair Value Measurements Using Fair Value Hierarchy		
			Level 1	Level 2	Level 3
Financial assets:					
Available-for-sale securities	\$10,111,759	\$10,111,759	\$10,111,759	\$ —	\$ —
Securities-held-to maturity	58,498,406	58,277,480	—	58,277,480	—
Derivative financial instruments	3,218,011	3,218,011	—	3,218,011	—
Financial liabilities:					
Derivative financial instruments	26,121,426	26,121,426	—	26,121,426	—

Available-for-sale securities: Fair values are approximated on current market quotes received from financial sources that trade such securities.

Securities-held-to maturity: Fair values are approximated on current market quotes received from financial sources that trade such securities and are based on prevailing market data and derived from third party proprietary models based on well recognized financial principles and reasonable estimates about relevant future market conditions.

Derivative financial instruments: Fair values are approximated on current market quotes received from financial sources that trade such securities and are based on prevailing market data and derived from third party proprietary models based on well recognized financial principles and reasonable estimates about relevant future market conditions. These items are included in other assets and other liabilities on the consolidated balance sheet.

Note 11 — Commitments and Contingencies

Contractual Commitments

As of June 30, 2008, the Company had the following material contractual obligations (payments in thousands):

Contractual Obligations	Payments Due by Period (1)						Total
	2008	2009	2010	2011	2012	Thereafter	
Notes payable (2)	\$ 117,790	\$ 83,908	\$ 384,190	\$ —	\$ —	\$ 49,500	\$ 635,388
Collateralized debt obligations (3)	6,360	96,493	96,493	303,470	626,833	—	1,129,649

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

Contractual Obligations	Payments Due by Period (1)						Total
	2008	2009	2010	2011	2012	Thereafter	
Repurchase agreements	43,383	115,210	40,163	—	—	—	198,756
Trust preferred securities	—	—	—	—	—	276,055	276,055
Outstanding unfunded commitments (4)	42,289	43,985	11,069	7,746	1,473	986	107,548
Totals	<u>\$200,030</u>	<u>\$344,648</u>	<u>\$536,760</u>	<u>\$311,248</u>	<u>\$628,174</u>	<u>\$326,536</u>	<u>\$2,347,396</u>

- (1) Represents amounts due based on contractual maturities.
- (2) Maturity date for Wachovia term and revolving facilities includes the one year extension option.
- (3) Comprised of \$279.3 million of CDO I debt, \$345.6 million of CDO II debt and \$504.7 million of CDO III debt with a weighted average remaining maturity of 2.02, 3.46 and 3.98 years, respectively, as of June 30, 2008.
- (4) In accordance with certain loans and investments, the Company has outstanding unfunded commitments of \$107.5 million as of June 30, 2008, that it is obligated to fund as the borrowers meet certain requirements. Specific requirements include, but are not limited to, property renovations, building construction, and building conversions based on criteria met by the borrower in accordance with the loan agreements.

Litigation

The Company currently is neither subject to any material litigation nor, to management's knowledge, is any material litigation currently threatened against the company.

Note 12 — Stockholders' Equity

Preferred Stock

Concurrent with the formation of the Company, ACM contributed a portfolio of structured finance investments and related debt to ARLP, the operating partnership of the Company, in exchange for 3,146,724 units of limited partnership interest in ARLP and warrants to purchase an additional 629,345 operating partnership units which were exercised in 2004. Concurrently, the Company, ARLP and ACM entered into a pairing agreement. Pursuant to the pairing agreement, each operating partnership unit issued to ACM and issuable to ACM upon the subsequent exercise of its warrants for additional operating partnership units was paired with one share of the Company's special voting preferred stock. Each share of special voting preferred stock entitled the holder to one vote on all matters submitted to a vote of the Company's stockholders. As of December 31, 2007, the Company had 3,776,069 shares issued and outstanding.

In June 2008, ACM exercised its right to redeem its 3,776,069 OP units in the Company's operating partnership for shares of the Company's common stock on a one-for-one basis. As a result, the special voting preferred shares paired with each OP unit, pursuant to a pairing agreement, were redeemed simultaneously and cancelled by the Company.

Common Stock

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

The Company paid its incentive compensation management fee to ACM in a combination of cash and shares of common stock during 2008. The following table presents the number of shares of common stock issued by the Company from January 1, 2008 through June 30, 2008 for the portion of its incentive compensation management fee paid in common stock:

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

<u>Issued</u>	<u>For the Quarter Ended</u>	<u>Number of Common Shares Issued</u>
February 2008	December 2007	86,772
May 2008	March 2008	55,532
	<u>Total</u>	<u>142,304</u>

In 2007, the Company filed a shelf registration statement on Form S-3 with the SEC under the 1933 Act with respect to an aggregate of \$500.0 million of debt securities, common stock, preferred stock, depositary shares and warrants that may be sold by the Company from time to time pursuant to Rule 415 of the 1933 Act. On April 19, 2007, the Commission declared this shelf registration statement effective. At June 30, 2008, the Company had \$425.3 million available under this shelf registration.

In June 2008, the Company issued 3,776,069 common shares upon the exchange of OP units by ACM. In connection with this transaction, the Company's Board of Directors approved a resolution of the Company's charter allowing ACM and Ivan Kaufman to own more than the 7% ownership limitation of the Company's outstanding common stock.

In addition, during the quarter, the Company issued 300,740 shares of common stock under its stock incentive plan and had 752 shares of common stock forfeited. The Company had 24,737,696 shares of common stock outstanding at June 30, 2008 and 20,519,335 shares of common stock outstanding at December 31, 2007.

Deferred Compensation

In April 2008, the Company issued an aggregate of 230,740 shares of restricted common stock under the 2003 Stock Incentive Plan, as amended in 2005 (the "Plan"), of which 216,740 shares were awarded to certain employees of the Company and ACM and 14,000 shares were issued to non-management members of the board of directors. One fifth of the 216,740 shares of restricted stock granted to each of the employees of the Company and ACM were vested as of the date of grant, the second one-fifth will vest in April 2009, the third one-fifth will vest in April 2010, the fourth one-fifth will vest in April 2011, and the remaining one-fifth will vest in April 2012. One third of the 14,000 shares of restricted stock granted to each director was vested as of the date of grant, another one third will vest in April 2009, and the remaining third will vest in April 2010.

In June 2008, the Company issued an aggregate of 70,000 shares of restricted common stock under the stock incentive plan to certain employees of the Company and ACM. One third of the 70,000 shares of restricted stock granted to each of the employees of the Company and ACM were vested as of the date of grant, another one third will vest in June 2009, and the remaining third will vest in June 2010.

In May 2008, 752 shares of unvested restricted common stock were forfeited. In addition, in May 2008, the Company's shareholders approved an amendment to the Plan to authorize an additional 400,000 shares of the Company's common stock reserved for issuance under the Plan.

Note 13 — Earnings Per Share

Earnings per share ("EPS") is computed in accordance with SFAS No. 128, Earnings Per Share. Basic earnings per share is calculated by dividing net income by the weighted average number of shares of common stock outstanding during each period inclusive of unvested restricted stock which participate fully in dividends. Diluted EPS is calculated by dividing income adjusted for minority interest by the weighted average number of shares of common stock outstanding plus the additional dilutive effect of common stock equivalents during each period. The Company's common stock equivalents are ARLP's operating partnership units and the potential settlement of incentive management fees in common stock.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

The following is a reconciliation of the numerator and denominator of the basic and diluted earnings per share computations for the three months ended June 30, 2008 and 2007.

	For the Three Months Ended June 30, 2008		For the Three Months Ended June 30, 2007	
	Basic	Diluted	Basic	Diluted
Net income	\$ 11,728,006	\$ 11,728,006	\$ 31,685,024	\$ 31,685,024
Add: income allocated to minority interest	—	2,117,464	—	6,638,020
Earnings per EPS calculation	<u>\$ 11,728,006</u>	<u>\$ 13,845,470</u>	<u>\$ 31,685,024</u>	<u>\$ 38,323,044</u>
Weighted average number of common shares outstanding	20,906,383	20,906,383	17,993,924	17,993,924
Weighted average number of operating partnership units	—	3,734,574	—	3,776,069
Dilutive effect of incentive management fee shares	—	80,703	—	103,329
Total weighted average common shares outstanding	<u>20,906,383</u>	<u>24,721,660</u>	<u>17,993,924</u>	<u>21,873,322</u>
Earnings per common share	<u>\$ 0.56</u>	<u>\$ 0.56</u>	<u>\$ 1.76</u>	<u>\$ 1.75</u>

The following is a reconciliation of the numerator and denominator of the basic and diluted earnings per share computations for the six months ended June 30, 2008 and 2007.

	For the Six Months Ended June 30, 2008		For the Six Months Ended June 30, 2007	
	Basic	Diluted	Basic	Diluted
Net income	\$ 24,432,797	\$ 24,432,797	\$ 48,448,605	\$ 48,448,605
Add: income allocated to minority interest	—	4,450,754	—	10,318,334
Earnings per EPS calculation	<u>\$ 24,432,797</u>	<u>\$ 28,883,551</u>	<u>\$ 48,448,605</u>	<u>\$ 58,766,939</u>
Weighted average number of common shares outstanding	20,739,081	20,739,081	17,590,860	17,590,860
Weighted average number of operating partnership units	—	3,755,321	—	3,776,069
Dilutive effect of incentive management fee shares	—	68,118	—	87,040
Total weighted average common shares outstanding	<u>20,739,081</u>	<u>24,562,520</u>	<u>17,590,860</u>	<u>21,453,969</u>
Earnings per common share	<u>\$ 1.18</u>	<u>\$ 1.18</u>	<u>\$ 2.75</u>	<u>\$ 2.74</u>

Note 14 — Related Party Transactions

At June 30, 2008, due to related party was \$7.9 million and consisted of \$8.8 million of management fees that were due to ACM and will be remitted in August 2008, which was partially offset by \$0.9 million of escrows due from ACM which were received by the Company in July 2008. At December 31, 2007, due to related party was \$2.4 million and consisted of \$3.2 million of management fees that were due to ACM and remitted in February 2008, which was partially offset by \$0.8 million of extension and filing fees received by ACM which were remitted to the Company in January 2008.

During 2006, the Company originated a \$7.2 million bridge loan and a \$0.3 million preferred equity investment secured by garden-style and townhouse apartments in South Carolina. The Company also had a 25.0%

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

carried profits interest in the borrowing entity. In January 2008, the borrowing entity refinanced the property through ACM's Fannie Mae program and the Company received \$0.3 million for its profits interest as well as full repayment of the \$0.3 million preferred equity investment and the \$7.0 million outstanding balance on the bridge loan. The Company retained the 25% carried profits interest.

In March 2008, ACM purchased from third party investors, investment grade CDO notes issued by subsidiaries of the Company, with an aggregate face value of \$11.5 million for \$5.0 million.

The Company is dependent upon its manager (ACM), with whom it has a conflict of interest, to provide services to the Company that are vital to its operations. The Company's chairman, chief executive officer and president, Mr. Ivan Kaufman, is also the chief executive officer and president of ACM, and, the Company's chief financial officer, Mr. Paul Elenio, is the chief financial officer of ACM. In addition, Mr. Kaufman and the Kaufman entities together beneficially own approximately 91% of the outstanding membership interests of ACM and certain of the Company's employees and directors, also hold an ownership interest in ACM. Furthermore, one of the Company's directors also serves as the trustee of one of the Kaufman entities that holds a majority of the outstanding membership interests in ACM and co-trustee of another Kaufman entity that owns an equity interest in ACM. ACM currently holds approximately 5.0 million common shares, representing 20.1% of the voting power of the Company's outstanding stock.

Note 15 — Distributions

On July 25, 2008, the Company declared distributions of \$0.62 per share of common stock, payable with respect to the three months ended June 30, 2008, to stockholders of record at the close of business on August 15, 2008. The Company intends to pay this distribution on August 26, 2008.

The following table presents dividends declared by the Company on its common stock from January 1, 2008 through June 30, 2008:

Declaration Date	For Quarter Ended	Record Date	Payment Date	Dividend Per Share
January 25, 2008	December 2007	February 15, 2008	February 26, 2008	\$0.62
April 25, 2008	March 2008	May 15, 2008	May 27, 2008	\$0.62

The Company is still in the process of finalizing taxable income for 2007, as the Company awaits final tax information from some of its equity investments that the Company does not control. The Company anticipates that based on tax projections and additional estimated tax losses from equity investments above previous projections, the Company does not expect to issue a special dividend in 2008 related to 2007 taxable income.

Note 16 — Management Agreement

The Company, ARLP and Arbor Realty SR, Inc. have entered into a management agreement with ACM, which provides that for performing services under the management agreement, the Company will pay ACM an incentive compensation fee and base management fee. The incentive compensation fee is calculated as 25% of the amount by which ARLP's funds from operations exceeds 9.5% return on invested funds or the Ten Year U.S. Treasury Rate plus 3.5%, whichever is greater, as described in the management agreement. This fee is subject to recalculation and reconciliation at fiscal year end in accordance with the management agreement.

ARBOR REALTY TRUST, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(Unaudited)

The following table sets forth the Company's base and incentive compensation management fees for the periods indicated:

Management Fees:	For the Three Months Ended		For the Six Months Ended	
	June 30,		June 30,	
	2008	2007	2008	2007
Base	\$ 900,924	\$ 758,830	\$ 1,799,928	\$ 1,435,645
Incentive compensation— expensed	1,252,914	9,886,235	2,933,344	14,083,102
Total expensed	\$2,153,838	\$ 10,645,065	\$ 4,733,272	\$15,518,747
Incentive compensation— deferred	7,292,448	—	7,292,448	—
Incentive compensation— prepaid	—	19,047,949	—	19,047,949
Total management fee	\$9,446,286	\$ 29,693,014	\$12,025,720	\$34,566,666

For the three months ended June 30, 2008 and 2007, the Company recorded \$0.9 million and \$0.8 million, respectively, of base management fees due to ACM of which \$0.3 million, were included in due to related party and paid in the month subsequent to the respective periods.

For the three months ended June 30, 2008, ACM earned an incentive compensation installment totaling \$8.5 million which was included in due to related party. Included in the \$8.5 million of incentive compensation was \$1.2 million recorded as management fee expense and \$7.3 million recorded as deferred management fee related to the incentive management fee earned from the monetization of the POM equity kicker transaction in June 2008. Upon the closing of this transaction, which is expected to occur on or before June 26, 2009, the Company will recognize the \$7.3 million as management fee expense. ACM intends to elect to be paid its incentive compensation management fee partially in 417,050 shares of common stock with the remainder to be paid in cash totaling \$4.8 million, payable in August 2008. For the three months ended June 30, 2007, ACM earned an incentive compensation installment totaling \$28.9 million which was included in due to related party. Included in the \$28.9 million of incentive compensation was \$9.9 million recorded as management fee expense and \$19.0 million recorded as deferred management fees related to the incentive management fee on the deferred gain recognized on the transfer of control of the 450 West 33rd Street property of one of the Company's equity affiliates.

For the six months ended June 30, 2008, ACM earned a base management fee of \$1.8 million and an incentive compensation installment totaling \$10.2 million. Included in the \$10.2 million of incentive compensation was \$2.9 million recorded as management fee expense and \$7.3 million recorded as deferred management fee related to the incentive management fee earned from the monetization of the POM equity kicker transaction in June 2008. For the six months ended June 30, 2007, ACM earned a base management fee of \$1.4 million and an incentive compensation installment totaling \$33.1 million. Included in the \$33.1 million of incentive compensation was \$14.1 million recorded as management fee expense and \$19.0 million recorded as deferred management fees related to the incentive management fee on the deferred gain recognized on the transfer of control of the 450 West 33rd Street property of one of the Company's equity affiliates.

Note 17 — Due to Borrowers

Due to borrowers represents borrowers' funds held by the Company to fund certain expenditures or to be released at the Company's discretion upon the occurrence of certain pre-specified events, and to serve as additional collateral for borrowers' loans. While retained, these balances earn interest in accordance with the specific loan terms they are associated with.

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

You should read the following discussion in conjunction with the unaudited consolidated interim financial statements, and related notes included herein.

Overview

We are a Maryland corporation that was formed in June 2003 to invest in multi-family and commercial real estate-related bridge loans, junior participating interests in first mortgages, mezzanine loans, preferred and direct equity and, in limited cases, discounted mortgage notes and other real estate-related assets, which we refer to collectively as structured finance investments. We have also invested in mortgage-related securities. We conduct substantially all of our operations through our operating partnership and its wholly-owned subsidiaries.

Our operating performance is primarily driven by the following factors:

- *Net interest income earned on our investments* — Net interest income represents the amount by which the interest income earned on our assets exceeds the interest expense incurred on our borrowings. If the yield earned on our assets decreases or the cost of borrowings increases, this will have a negative impact on earnings. However, if the yield earned on our assets increases or the cost of borrowings decreases, this will have a positive impact on earnings. Net interest income is also directly impacted by the size of our asset portfolio.
- *Credit quality of our assets* — Effective asset and portfolio management is essential to maximizing the performance and value of a real estate/mortgage investment. Maintaining the credit quality of our loans and investments is of critical importance. Loans that do not perform in accordance with their terms may have a negative impact on earnings.
- *Cost control* — We seek to minimize our operating costs, which consist primarily of employee compensation and related costs, management fees and other general and administrative expenses. As the size of the portfolio increases or there are increases in foreclosures and non-performing loans and investments, certain of these expenses, particularly employee compensation expenses and asset management related expenses, may increase.

We are organized and conduct our operations to qualify as a real estate investment trust ("REIT") for federal income tax purposes. A REIT is generally not subject to federal income tax on its REIT—taxable income that it distributes to its stockholders, provided that it distributes at least 90% of its REIT—taxable income and meets certain other requirements. Certain of our assets that produce non-qualifying income are owned by our taxable REIT subsidiaries, the income of which are subject to federal and state income taxes. We recorded a \$15.1 million provision for income taxes related to the assets that are held in taxable REIT subsidiaries during the six months ended June 30, 2007. No such provision for income taxes had been recognized for the six months ended June 30, 2008.

Sources of Operating Revenues

We derive our operating revenues primarily through interest received from making real estate-related bridge, mezzanine and junior participation loans and preferred equity investments. For the three and six months ended June 30, 2008, interest income earned on these loans and investments represented approximately 98% and 99% of our total revenues, respectively. For the three and six months ended June 30, 2007, interest income earned on these loans and investments represented approximately 93% and 85% of our total revenues, respectively.

Interest income may also be derived from profits of equity participation interests. For the six months ended June 30, 2008, interest on these investments represented approximately less than 1% of our total revenues. No such income had been recognized for the three months ended June 30, 2008. For the three and six months ended June 30, 2007, interest on these investments represented approximately 7% and 15% of our total revenues, respectively.

[Table of Contents](#)

We derived interest income from our investments in CRE collateralized debt obligation bond securities. For the three months and six months ended June 30, 2008, interest on these investments represented approximately 1% and less than 1% of our total revenues, respectively. For the three and six months ended June 30, 2007, no such investments were made.

Additionally, we derive operating revenues from other income that represents loan structuring and miscellaneous asset management fees associated with our loans and investments portfolio. For the three and six months ended June 30, 2008 and June 30, 2007, revenue from other income represented less than 1% of our total revenues.

Income or Loss from Equity Affiliates and Gain on Sale of Loans and Real Estate

We derive income or losses from equity affiliates relating to joint ventures that were formed with equity partners to acquire, develop and/or sell real estate assets. These joint ventures are not majority owned or controlled by us, and are not consolidated in our financial statements. These investments are recorded under either the equity or cost method of accounting as appropriate. We record our share of net income and losses from the underlying properties on a single line item in the consolidated income statements as income from equity affiliates. For the six months ended June 30, 2008, loss from equity affiliates totaled approximately \$0.6 million. For the six months ended June 30, 2007, income from equity affiliates totaled approximately \$26.0 million. The \$26.0 million during the six months ended June 30, 2007 included a \$24.2 million gain recognized on the sale of one of the properties of one of our equity affiliates and \$1.8 million of income from excess proceeds received from the refinance of properties in the portfolio of another of our equity affiliates during the six months ended June 30, 2007.

We also may derive income from the gain on sale of loans and real estate. We may acquire (1) real estate for our own investment and, upon stabilization, disposition at an anticipated return and (2) real estate notes generally at a discount from lenders in situations where the borrower wishes to restructure and reposition its short term debt and the lender wishes to divest certain assets from its portfolio. No such income has been recorded to date.

Critical Accounting Policies

Please refer to the section of our Annual Report on Form 10-K for the year ended December 31, 2007 entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Significant Accounting Estimates and Critical Accounting Policies” for a discussion of our critical accounting policies. During the six months ended June 30, 2008, there were no material changes to these policies, except for the updates described below.

Revenue Recognition

Interest income is recognized on the accrual basis as it is earned from loans, investments and securities. In many instances, the borrower pays an additional amount of interest at the time the loan is closed, an origination fee, and deferred interest upon maturity. In some cases, interest income may also include the amortization or accretion of premiums and discounts arising from the purchase or origination of the loan or security. This additional income, net of any direct loan origination costs incurred, is deferred and accreted into interest income on an effective yield or “interest” method adjusted for actual prepayment activity over the life of the related loan or security as a yield adjustment. Income recognition is suspended for loans when in the opinion of management a full recovery of income and principal becomes doubtful. Income recognition is resumed when the loan becomes contractually current and performance is demonstrated to be resumed. Several of the loans provide for accrual of interest at specified rates, which differ from current payment terms. Interest is recognized on such loans at the accrual rate subject to management’s determination that accrued interest and outstanding principal are ultimately collectible, based on the underlying collateral and operations of the borrower. If management cannot make this determination regarding collectibility, interest income above the current pay rate is recognized only upon actual receipt. Additionally, interest income is recorded when earned from equity participation interests, referred to as equity kickers. These equity kickers have the potential to generate additional revenues to us as a result of excess cash flows being distributed and/or as appreciated properties are sold or refinanced. We recorded interest on such loans and investments of \$0.3 million for the six months ended June 30, 2008, compared to \$23.0 million for the six months ended June 30, 2007. For the three months ended June 30, 2007, we recorded \$6.2 million of interest from such loans and investments. No such income had been recognized for the three months ended June 30, 2008.

Derivatives and Hedging Activities

In accordance with SFAS No. 133, the carrying values of interest rate swaps and the underlying hedged liabilities are reflected at their fair value. As of December 31, 2007 we retained the services of Chatham Financial Corporation, a Statement on Auditing Standards No. 70 (“SAS 70”), “Service Organizations” compliant, third party financial services company to determine these fair values. Changes in the fair value of these derivatives are either offset against the change in the fair value of the hedged liability through earnings or recognized in other comprehensive income (loss) until the hedged item is recognized in earnings. The ineffective portion of a derivative’s change in fair value is immediately recognized in earnings. Derivatives that do not qualify for cash flow hedge accounting treatment are adjusted to fair value through earnings.

During the six months ended June 30, 2008, we entered into six additional interest rate swaps, respectively, that qualify as cash flow hedges, having a total combined notional value of approximately \$121.6 million. No such swaps had been entered into for the three months ended June 30, 2008. The fair value of our qualifying hedge portfolio has increased by approximately \$3.8 million from December 31, 2007 as a result of these additional swaps and a change in the projected LIBOR rates.

Because the valuations of our hedging activities are based on estimates, the fair value may change if our estimates are inaccurate. For the effect of hypothetical changes in market interest rates on our interest rate swaps, see “Interest Rate Risk” in “Quantitative and Qualitative Disclosures About Market Risk”, set forth in Item 7A hereof.

Recently Issued Accounting Pronouncements

For a discussion of the impact of new accounting pronouncements on our financial condition or results of operations, see Note 2 of the “Notes to the Consolidated Financial Statements” set forth in Item 1 hereof.

Changes in Financial Condition

Our loan and investment portfolio balance at June 30, 2008 was \$2.5 billion, with a weighted average current interest pay rate of 7.07% as compared to \$2.6 billion, with a weighted average current interest pay rate of 8.18% at December 31, 2007. At June 30, 2008, advances on financing facilities totaled \$2.2 billion, with a weighted average funding cost of 4.85% as compared to \$2.3 billion, with a weighted average funding cost of 6.16% at December 31, 2007.

During the quarter ended June 30, 2008, we originated two new bridge loans totaling \$6.5 million and purchased seven CRE collateralized debt obligation bond securities at a discounted price of approximately \$58.1 million with a face amount of approximately \$82.7 million. During the quarter, eight loans paid off on properties that were either sold or refinanced by a third party with an outstanding balance of \$127.4 million, three loans partially repaid totaling \$24.1 million and three loans were either refinanced or modified during the quarter totaling \$86.0 million. Of the loans refinanced or modified, one loan totaling \$14.5 million was scheduled to repay during the quarter, and another loan totaling approximately \$63.5 million has a \$1.0 million loan loss reserve, which was recorded in the first quarter of 2008. In addition, three loans totaling approximately \$94.7 million were extended during the quarter in accordance with the extension options of the corresponding loan agreements.

Other assets increased \$12.7 million, or 15%, to \$96.4 million at June 30, 2008 compared to \$83.7 million at December 31, 2007. The increase was primarily due to a \$16.5 million third party member receivable recorded during the second quarter of 2008 in connection with the POM transaction. This amount reflects the third party member’s pro-rata portion of the \$49.5 million debt recorded from the consolidated entity in notes payable. This was partially offset by a decrease of \$3.2 million in deferred financing costs associated with the amortization of costs associated with our financing sources.

Securities held to maturity were \$58.5 million at June 30, 2008, and reflects the purchase of \$82.7 million of investment grade CRE collateralized debt obligation bonds for \$58.1 million during the second quarter. The \$24.6

[Table of Contents](#)

million discount will be accreted into interest income on an effective yield adjusted for actual prepayment activity over the average life of the related security as a yield adjustment. We did not have any securities held-to-maturity at December 31, 2007. See Note 5 of the “Notes to the Consolidated Financial Statements” set forth in Item 1 hereof for a further description of these transactions.

Real estate owned, net was \$46.9 million at June 30, 2008, representing the fair market value of an office property in which we foreclosed on during the second quarter of 2008. In addition, we recorded a \$41.4 million first lien on the property in mortgage notes payable. See Note 3 of the “Notes to the Consolidated Financial Statements” set forth in Item 1 hereof for a further description of these transactions.

Deferred management fee was \$7.3 million at June 30, 2008 which relates to the incentive management fee on the \$33 million of cash received in June 2008 from the agreement to transfer 16.67% of our 24.17% interest in Prime Outlets Member LLC (“POM”), one of our equity affiliates. Upon the closing of this transaction, which is expected to occur on or before June 26, 2009, we will exchange our 16.67% interest in POM for approximately \$37 million of preferred and common operating partnership units in another REIT, at which time the deferred management fee will be recognized as expense. See Note 6 of the “Notes to the Consolidated Financial Statements” set forth in Item 1 hereof for further description of this transaction.

Other liabilities decreased \$9.2 million, or 14%, from \$67.4 million at December 31, 2007 compared to \$58.2 million at June 30, 2008. The decrease was primarily due to \$6.6 million decrease in accrued interest payable primarily due to a reduction in LIBOR rates and a decline in the outstanding balance of our financing facilities. This was combined with a \$1.8 million decrease in margin loan balances on our available for sale securities and interest rate swaps cash collateral.

In June 2008, ACM, our manager, exercised its right to redeem its 3,776,069 operating partnership units in the operating partnership for shares of our common stock on a one-for-one basis. As a result, ACM’s operating partnership ownership interest in us was reduced to zero and the balance of minority interest was charged directly to equity in additional paid-in capital, as of June 30, 2008. See Notes 8 and 12 of the “Notes to the Consolidated Financial Statements” set forth in Item 1 hereof for a further description of this transaction.

In June 2008, we issued an aggregate of 70,000 shares of restricted common stock under the stock incentive plan to certain employees of ours and ACM. One third of the 70,000 shares of restricted stock granted to each of the employees were vested as of the date of grant, another one third will vest in June 2009, and the remaining third will vest in June 2010.

In April 2008, 14,000 restricted shares were issued to non-management members of the board of directors under the stock incentive plan. One third of the restricted stock granted was vested as of the date of grant, another one third will vest in April 2009, and the remaining third will vest in April 2010.

In April 2008, we issued 216,740 shares of restricted common stock under the stock incentive plan to certain employees of ours and ACM. One fifth of the restricted stock granted to each of these employees were vested as of the date of grant, the second one-fifth will vest in April 2009, the third one-fifth will vest in April 2010, the fourth one-fifth will vest in April 2011, and the remaining one-fifth will vest in April 2012.

ACM was paid an aggregate of 142,304 shares of common stock for its fourth quarter 2007 and first quarter 2008 incentive management fees during the six months ended June 30, 2008. Furthermore, in August 2008, ACM will be paid a portion of its second quarter 2008 incentive management fee in 417,050 shares of common stock.

[Table of Contents](#)

Comparison of Results of Operations for the Three Months Ended June 30, 2008 and 2007

The following table sets forth our results of operations for the three months ended June 30, 2008 and 2007:

	Three Months Ended June 30,		Increase/(Decrease)	
	2008	2007	Amount	Percent
	(Unaudited)			
Revenue:				
Interest income	\$51,869,164	\$74,800,274	\$(22,931,110)	(31)%
Other income	28,629	17,186	11,443	67%
Total revenue	51,897,793	74,817,460	(22,919,667)	(31)%
Expenses:				
Interest expense	27,857,322	38,527,983	(10,670,661)	(28)%
Employee compensation and benefits	2,686,002	2,753,662	(67,660)	(2)%
Selling and administrative	2,793,161	1,593,494	1,199,667	75%
Provision for loan losses	2,000,000	—	2,000,000	nm
Management fee — related party	2,153,838	10,645,065	(8,491,227)	(80)%
Total expenses	37,490,323	53,520,204	(16,029,881)	(30)%
Income before income from equity affiliates, minority interest and provision for income taxes	14,407,470	21,297,256	(6,889,786)	(32)%
(Loss) income from equity affiliates	(562,000)	26,025,788	(26,587,788)	nm
Income before minority interest and provision for income taxes	13,845,470	47,323,044	(33,477,574)	(71)%
Income allocated to minority interest	2,117,464	6,638,020	(4,520,556)	(68)%
Income before provision for income taxes	11,728,006	40,685,024	(28,957,018)	(71)%
Provision for income taxes	—	9,000,000	(9,000,000)	nm
Net income	\$11,728,006	\$31,685,024	\$(19,957,018)	(63)%
nm — not meaningful				

Revenue

Interest income decreased \$22.9 million, or 31%, to \$51.9 million for the three months ended June 30, 2008 from \$74.8 million for the three months ended June 30, 2007. This decrease was due in part to the recognition of \$14.6 million of interest income from profits and equity interests from certain of our loans and investments in equity affiliates during the three months ended June 30, 2007.

Excluding these transactions, interest income decreased \$8.3 million, or 14%, compared to the same period in the prior year. This decrease was primarily due to a 17% decrease in the average yield on assets from 9.55% for the three months ended June 30, 2007 to 7.91% for the three months ended June 30, 2008. This decrease in yield was the result of a decrease in LIBOR over the same period and a reduction in the yield on new originations compared to higher yielding loan payoffs from the same period in 2007. This was partially offset by a portion of our portfolio having LIBOR floors and fixed rates of interest, as well as a 6% increase in the average balance of loans and investments from \$2.4 billion for the three months ended June 30, 2007 to \$2.6 billion for the three months ended June 30, 2008 due to increased loan and investment originations from period to period. In addition, interest income from cash equivalents decreased \$1.2 million to \$1.2 million for the three months ended June 30, 2008 compared to \$2.4 million for the three months ended June 30, 2007 as a result of decreased average restricted and unrestricted cash balances, as well as decreases in interest rates from 2007 to 2008.

[Table of Contents](#)

Other income increased \$11,443 to \$28,629 for the three months ended June 30, 2008 from \$17,186 for the three months ended June 30, 2007. This is primarily due to increased miscellaneous asset management fees on our loan and investment portfolio.

Expenses

Interest expense decreased \$10.7 million, or 28%, to \$27.9 million for the three months ended June 30, 2008 from \$38.5 million for the three months ended June 30, 2007. This decrease was primarily due to a 26% decrease in the average cost of these borrowings from 6.82% for the three months ended June 30, 2007 to 5.06% for the three months ended June 30, 2008 due to a reduction in average LIBOR on the portion of our debt that was floating over the same period. In addition, there was a 3% decrease in the average balance of our debt facilities from \$2.3 billion for the three months ended June 30, 2007 to \$2.2 billion for the three months ended June 30, 2008 as a result of decreased leverage on our portfolio due to the paying down of certain outstanding indebtedness from available capital.

Employee compensation and benefits expense decreased \$0.1 million, or 2%, to \$2.7 million for the three months ended June 30, 2008 from \$2.8 million for the three months ended June 30, 2007. This decrease was primarily due to a decrease in employee salaries and benefits primarily offset by increased costs related to restricted stock awards granted to employees. These expenses represent salaries, benefits, stock-based compensation related to employees, and incentive compensation for those employed by us during these periods.

Selling and administrative expense increased \$1.2 million, or 75%, to \$2.8 million for the three months ended June 30, 2008 from \$1.6 million for the three months ended June 30, 2007. These costs include, but are not limited to, professional and consulting fees, marketing costs, insurance expense, director's fees, licensing fees, travel and placement fees, and stock-based compensation relating to the cost of restricted stock granted to our directors and certain employees of our manager. The increase was primarily due to expenses related to the POM Outlets transaction and other increases in professional fees including general corporate legal expenses. In addition, we recognized a loss of \$0.2 million from the sale of property securing the Windrush Village bridge loan. See Note 3 of the "Notes to the Consolidated Financial Statements" set forth in Item 1 hereof for further details on this transaction.

Provision for loan losses totaled \$2.0 million for the three months ended June 30, 2008, and there was no provision for loan losses for the three months ended June 30, 2007. The provision recorded was based on our normal quarterly loan review at June 30, 2008, where it was determined that one loan with an outstanding principal balance of \$9.9 million became impaired during the quarter. We performed an evaluation of the loan and determined that the fair value of the underlying collateral securing the impaired loan was less than the net carrying value of the loan resulting in us recording a \$2.0 million provision for loan loss.

Management fees decreased \$8.5 million to \$2.1 million for the three months ended June 30, 2008 from \$10.6 million for the three months ended June 30, 2007. These amounts represent compensation in the form of base management fees and incentive management fees as provided for in the management agreement with our manager. The incentive compensation management fee expense decreased by \$8.6 million, or 87%, to \$1.3 million for the three months ended June 30, 2008 from \$9.9 million for the three months ended June 30, 2007. The decrease was primarily due to the recognition of \$14.6 million of interest income from profits and equity interests and \$26.0 million of income from equity affiliates during the three months ended June 30, 2007. The base management fee expense increased by \$0.1 million, or 19%, to \$0.9 million for the three months ended June 30, 2008 compared to \$0.8 million for the three months ended June 30, 2007. This increase is primarily due to increased stockholders' equity directly attributable to greater undistributed profits and capital raised from the June 2007 public offering of our common stock.

Income or (Losses) From Equity Affiliates

Losses from equity affiliates totaled \$0.6 million for the three months ended June 30, 2008. Income from equity affiliates totaled \$26.0 million for the three months ended June 30, 2007. This decrease was primarily due to the recognition of a \$24.2 million gain on the sale of one of the properties of one of our equity affiliates and \$1.8 million of income from excess proceeds received from the refinance of properties in the portfolio of another of our

[Table of Contents](#)

investments in equity affiliates during the three months ended June 30, 2007. The \$0.6 million loss recorded during the three months ended June 30, 2008, reflects a portion of a joint venture's losses from a \$13.2 million equity investment.

Income Allocated to Minority Interest

Income allocated to minority interest decreased \$4.5 million, or 68%, to \$2.1 million for the three months ended June 30, 2008 from \$6.6 million for the three months ended June 30, 2007. These amounts represent the portion of our income allocated to our manager. This decrease was primarily due to a 64% decrease in income before minority interest reduced by the provision for income taxes over the same period and a decrease in our manager's limited partnership interest in us. Our manager had a weighted average limited partnership interest of 15.2% in our operating partnership for the three months ended June 30, 2008 compared to 17.4% for the three months ended June 30, 2007. In June 2008, our manager, exercised its right to redeem its 3,776,069 operating partnership units in our operating partnership for shares of our common stock on a one-for-one basis. As a result, our manager's operating partnership ownership interest percentage was reduced to zero at June 30, 2008.

Provision for Income Taxes

We are organized and conduct our operations to qualify as a REIT for federal income tax purposes. As a REIT, we are generally not subject to federal income tax on our REIT—taxable income that we distribute to our stockholders, provided that we distribute at least 90% of our REIT—taxable income and meet certain other requirements. As of June 30, 2008 and 2007, we were in compliance with all REIT requirements and, therefore, have not provided for income tax expense on our REIT—taxable income for the three months ended June 30, 2008 and 2007.

Certain of our assets that produce non-qualifying income are owned by our taxable REIT subsidiaries, the income of which is subject to federal and state income taxes. During the three months ended June 30, 2007, we recorded a \$9.0 million provision on income from these taxable REIT subsidiaries. No such provision had been recognized for the three months ended June 30, 2008. The provision for the three months ended June 30, 2007 resulted from a \$24.2 million gain recognized on the sale of property of one of our investment in equity affiliates representing the portion attributable to the 20% equity interest in the borrowing entity.

[Table of Contents](#)

Comparison of Results of Operations for the Six Months Ended June 30, 2008 and 2007

The following table sets forth our results of operations for the six months ended June 30, 2008 and 2007:

	Six Months Ended June 30,		Increase/(Decrease)	
	2008	2007	Amount	Percent
	(Unaudited)			
Revenue:				
Interest income	\$ 107,285,494	\$ 141,260,927	\$(33,975,433)	(24)%
Other income	49,322	23,356	25,966	111%
Total revenue	107,334,816	141,284,283	(33,949,467)	(24)%
Expenses:				
Interest expense	59,161,421	70,640,502	(11,479,081)	(16)%
Employee compensation and benefits	4,663,345	4,484,017	179,328	4%
Selling and administrative	4,331,227	2,814,866	1,516,361	54%
Provision for loan losses	5,000,000	—	5,000,000	nm
Management fee — related party	4,733,272	15,518,747	(10,785,475)	(69)%
Total expenses	77,889,265	93,458,132	(15,568,867)	(17)%
Income before income from equity affiliates, minority interest and provision for income taxes	29,445,551	47,826,151	(18,380,600)	(38)%
Income from equity affiliates	(562,000)	26,025,788	(26,587,788)	nm
Income before minority interest and provision for income taxes	28,883,551	73,851,939	(44,968,388)	(61)%
Income allocated to minority interest	4,450,754	10,318,334	(5,867,580)	(57)%
Income before provision for income taxes	24,432,797	63,533,605	(39,100,808)	(62)%
Provision for income taxes	—	15,085,000	(15,085,000)	nm
Net income	<u>\$ 24,432,797</u>	<u>\$ 48,448,605</u>	<u>\$(24,015,808)</u>	<u>(50)%</u>
nm — not meaningful				

Revenue

Interest income decreased \$34.0 million, or 24%, to \$107.3 million for the six months ended June 30, 2008 from \$141.3 million for the six months ended June 30, 2007. This decrease was due in part to the recognition of \$0.3 million of interest income from profits and equity interests from certain of our loans and investments in equity affiliates during the six months ended June 30, 2008, as compared to \$30.6 million during the six months ended June 30, 2007.

Excluding these transactions, interest income decreased \$3.7 million, or 3%, compared to the same period of the prior year. This was primarily due to a 15% decrease in the average yield on the assets from 9.61% for the six months ended June 30, 2007 to 8.13% for the six months ended June 30, 2008. This decrease in yield was the result of a decrease in LIBOR over the same period and a reduction in the yield on new originations compared to higher yielding loan payoffs from the same period in 2007. This was largely offset by a portion of our portfolio having LIBOR floors and fixed rates of interest, as well as a 15% increase in the average balance of loans and investments from \$2.2 billion for the six months ended June 30, 2007 to \$2.6 billion for the six months ended June 30, 2008 due

[Table of Contents](#)

to increased loan and investment originations. In addition, interest income from cash equivalents decreased \$1.0 million to \$3.0 million for the six months ended June 30, 2008 compared to \$4.0 million for the six months ended June 30, 2007 as a result of decreased average restricted and unrestricted cash balances.

Other income increased \$25,966, to \$49,322 for the six months ended June 30, 2008 from \$23,356 for the six months ended June 30, 2007. This was primarily due to increased miscellaneous asset management fees on our loan and investment portfolio.

Expenses

Interest expense decreased \$11.5 million, or 16%, to \$59.2 million for the six months ended June 30, 2008 from \$70.6 million for the six months ended June 30, 2007. This decrease was primarily due to a 22% decrease in the average cost of these borrowings from 6.85% for the six months ended June 30, 2007 to 5.35% for the six months ended June 30, 2008 due to a reduction in average LIBOR on the portion of our debt that was floating over the same period. This was partially offset by a 7% increase in the average balance of our debt facilities from \$2.1 billion for the six months ended June 30, 2007 to \$2.2 billion for the six months ended June 30, 2008 as a result of increased portfolio growth and financing facilities.

Employee compensation and benefits expense increased \$0.2 million, or 4%, to \$4.7 million for the six months ended June 30, 2008 from \$4.5 million for the six months ended June 30, 2007. This slight increase was primarily due to increases in costs related to restricted stock awards granted to employees. These expenses represent salaries, benefits, stock-based compensation related to employees, and incentive compensation for those employed by us during these periods.

Selling and administrative expense increased \$1.5 million, or 54%, to \$4.3 million for the six months ended June 30, 2008 from \$2.8 million for the six months ended June 30, 2007. These costs include, but are not limited to, professional and consulting fees, marketing costs, insurance expense, directors' fees, licensing fees, travel and placement fees, and stock-based compensation relating to the cost of restricted stock granted to our directors and certain employees of our manager. The increase was primarily due to expenses related to the Prime Outlets transaction and other increases in professional fees including general corporate legal expenses. This increase was also due to \$0.4 million of losses recognized from the sales of two properties securing two bridge loans during the six months ended June 30, 2008. See Note 3 of the "Notes to the Consolidated Financial Statements" set forth in Item 1 hereof for further details on these transactions.

Provision for loan losses totaled \$5.0 million for the six months ended June 30, 2008, and there was no provision for loan losses for the six months ended June 30, 2007. The provision recorded was based on our normal quarterly loan reviews during the period, where it was determined that four loans with an aggregate outstanding principal balance of \$80.3 million became impaired during the first six months of 2008. We performed an evaluation of the loans and determined that the fair value of the underlying collateral securing the impaired loans was less than the net carrying value of the loan resulting in us recording a \$5.0 million provision for loan losses.

Management fees decreased \$10.8 million, or 69%, to \$4.7 million for the six months ended June 30, 2008 from \$15.5 million for the six months ended June 30, 2007. These amounts represent compensation in the form of base management fees and incentive management fees as provided for in the management agreement with our manager. The incentive management fees decreased by \$11.2 million, or 79%, to \$2.9 million for the six months ended June 30, 2008 from \$14.1 million for the six months ended June 30, 2007. The decrease was primarily due to the recognition of \$0.3 million of interest income from profits and equity interests during the six months ended June 30, 2008 compared to \$30.6 million of interest income from profits and equity interests and \$26.0 million of income from equity affiliates during the six months ended June 30, 2007. The base management fees increased by \$0.4 million, or 25%, to \$1.8 million for the six months ended June 30, 2008 from \$1.4 million for the six months ended June 30, 2007. This increase is primarily due to increased stockholders' equity directly attributable to greater undistributed profits and capital raised from the June 2007 public offering of our common stock.

[Table of Contents](#)

Income or (Losses) From Equity Affiliates

Losses from equity affiliates totaled \$0.6 million for the six months ended June 30, 2008. Income from equity affiliates totaled \$26.0 million for the six months ended June 30, 2007. This decrease was primarily due to a \$24.2 million gain recognized on the sale of one of the properties of one of our equity affiliates and \$1.8 million of income from excess proceeds received from the refinance of properties in the portfolio of another of our investments in equity affiliates during the six months ended June 30, 2007. The \$0.6 million loss recorded during the six months ended June 30, 2008, reflects a portion of the joint venture's losses from a \$13.2 million equity investment.

Income Allocated to Minority Interest

Income allocated to minority interest decreased by \$5.9 million, or 57%, to \$4.4 million for the six months ended June 30, 2008 from \$10.3 million for the six months ended June 30, 2007. These amounts represent the portion of our income allocated to our manager. This decrease was primarily due to a 51% decrease in income before minority interest reduced by the provision for income taxes over the same periods and a decrease in our manager's limited partnership interest in us. Our manager had a weighted average limited partnership interest of 15.3% in our operating partnership for the six months ended June 30, 2008 compared to 17.7% for the six months ended June 30, 2007. In June 2008, our manager, exercised its right to redeem its 3,776,069 operating partnership units in our operating partnership for shares of our common stock on a one-for-one basis. As a result, our manager's operating partnership ownership interest percentage was reduced to zero at June 30, 2008.

Provision for Income Taxes

We are organized and conduct our operations to qualify as a REIT for federal income tax purposes. As a REIT, we are generally not subject to federal income tax on our REIT—taxable income that we distribute to our stockholders, provided that we distribute at least 90% of our REIT—taxable income and meet certain other requirements. As of June 30, 2008 and 2007, we were in compliance with all REIT requirements and, therefore, have not provided for income tax expense on our REIT—taxable income for the six months ended June 30, 2008 and 2007.

Certain of our assets that produce non-qualifying income are owned by our taxable REIT subsidiaries, the income of which are subject to federal and state income taxes. During the six months ended June 30, 2007, we recorded a \$15.1 million provision on income from these taxable REIT subsidiaries. No such provision had been recognized for the six months ended June 30, 2008. The provision for the six months ended June 30, 2007 resulted from a \$16.0 million distribution received representing the portion attributable to the 33.33% profits interest in a borrowing entity and a \$24.2 million gain recognized on the sale of property of one of our investments in equity affiliates representing the portion attributable to the 20.0% equity interest.

Liquidity and Capital Resources

Sources of Liquidity

Liquidity is a measurement of the ability to meet potential cash requirements. Our short-term and long-term liquidity needs include ongoing commitments to repay borrowings, fund future loans and investments, fund operating costs and distributions to our stockholders as well as other general business needs. Our primary sources of funds for liquidity consist of proceeds from equity offerings, debt facilities and cash flows from operations. Our equity sources consist of funds raised from our private equity offering in July 2003, net proceeds from our initial public offering of our common stock in April 2004, net proceeds from our public offering of our common stock in June 2007 and depending on market conditions, proceeds from capital market transactions including the future issuance of common, convertible and/or preferred equity securities. Our debt facilities include the issuance of floating rate notes resulting from our CDOs, the issuance of junior subordinated notes to subsidiary trusts issuing preferred securities and borrowings under credit agreements. Net cash provided by operating activities include interest income from our loan and investment portfolio reduced by interest expense on our debt facilities, cash from equity participation interests, repayments of outstanding loans and investments and funds from junior loan participation arrangements.

[Table of Contents](#)

We believe our existing sources of funds will be adequate for purposes of meeting our short-term and long-term liquidity needs. Our loans and investments are financed under existing credit facilities and their credit status is continuously monitored; therefore, these loans and investments are expected to generate a generally stable return. Our ability to meet our long-term liquidity and capital resource requirements is subject to obtaining additional debt and equity financing. If we are unable to renew our sources of financing on substantially similar terms or at all, it would have an adverse effect on our business and results of operations. Any decision by our lenders and investors to enter into such transactions with us will depend upon a number of factors, such as our financial performance, compliance with the terms of our existing credit arrangements, industry or market trends, the general availability of and rates applicable to financing transactions, such lenders' and investors' resources and policies concerning the terms under which they make such capital commitments and the relative attractiveness of alternative investment or lending opportunities.

To maintain our status as a REIT under the Internal Revenue Code, we must distribute annually at least 90% of our REIT—taxable income. These distribution requirements limit our ability to retain earnings and thereby replenish or increase capital for operations. However, we believe that our capital resources and access to financing will provide us with financial flexibility and market responsiveness at levels sufficient to meet current and anticipated capital requirements, including expected new lending and investment opportunities.

Equity Offerings

Our authorized capital provides for the issuance of up to 500 million shares of common stock, par value \$0.01 per share, and 100 million shares of preferred stock, par value \$0.01 per share.

In March 2007, we filed a shelf registration statement on Form S-3 with the SEC under the 1933 Act with respect to an aggregate of \$500.0 million of debt securities, common stock, preferred stock, depository shares and warrants, that may be sold by us from time to time pursuant to Rule 415 of the 1933 Act. On April 19, 2007, the Commission declared this shelf registration statement effective.

In June 2007, we sold 2,700,000 shares of our common stock registered on the shelf registration statement in a public offering at a price of \$27.65 per share, for net proceeds of approximately \$73.6 million after deducting the underwriting discount and the other estimated offering expenses. We used the proceeds to pay down debt and finance our loan and investment portfolio. The underwriters did not exercise their over allotment option for additional shares. At June 30, 2008, we had \$425.3 million available under this shelf registration and 24,737,696 shares outstanding.

Debt Facilities

We also maintain liquidity through two term credit agreements, one of which has a revolving credit component, two master repurchase agreements, one working capital facility, one notes payable, one junior loan participation and one bridge loan warehousing credit agreement with six different financial institutions or companies. In addition, we have issued three collateralized debt obligations (“CDOs”) and nine separate junior subordinated notes. London inter-bank offered rate, or LIBOR, refers to one-month LIBOR unless specifically stated. As of June 30, 2008, these facilities had an aggregate capacity of \$2.5 billion and borrowings were approximately \$2.2 billion.

[Table of Contents](#)

The following is a summary of our debt facilities as of June 30, 2008:

Debt Facilities	At June 30, 2008			Maturity Dates
	Commitment	Debt Carrying Value	Available	
Repurchase agreements. Interest is variable based on pricing over LIBOR	\$ 283,545,818	\$ 198,755,637	\$ 84,790,181	2008 — 2010
Collateralized debt obligations. Interest is variable based on pricing over three-month LIBOR	1,172,449,000	1,129,649,000	42,800,000	2011 — 2013
Junior subordinated notes. Interest is variable based on pricing over three-month LIBOR	276,055,000	276,055,000	—	2034 — 2037
Notes payable. Interest is variable based on pricing over Prime or LIBOR	<u>793,001,538</u>	<u>635,388,432</u>	<u>157,613,106</u>	2008 — 2013
	<u>\$ 2,525,051,356</u>	<u>\$ 2,239,848,069</u>	<u>\$ 285,203,287</u>	

These debt facilities are described in further detail in Note 6 of the “Notes to the Consolidated Financial Statements” set forth in Item 1 hereof.

Repurchase Agreements

Repurchase obligation financings provide us with a revolving component to our debt structure. Repurchase agreements provide stand alone financing for certain assets and interim, or warehouse financing, for assets that we plan to contribute to our CDOs. At June 30, 2008, the aggregate outstanding balance under these facilities was \$198.8 million.

We have a \$200.0 million repurchase agreement with a financial institution, effective October 2006, which was amended in December 2007 to increase the committed amount of the facility to \$200.0 million from \$150.0 million. The agreement has a term expiring in October 2009 and bears interest at pricing over LIBOR, varying on the type of asset financed. At June 30, 2008, the outstanding balance under this facility was \$115.2 million with a current weighted average note rate of 3.54%.

We have a \$100.0 million repurchase agreement with a second financial institution that was amended in September 2007 from a \$50.0 million warehouse credit facility. The amendment changed the form of the warehouse credit facility to a repurchase agreement, increased the committed amount of the facility to \$100.0 million, and extended the maturity date to September 2008. The repurchase agreement facility bears interest at pricing over LIBOR. In January 2008, we were notified that no further advances could be taken under this facility. The facility matures in September 2008 and under the terms of the repurchase agreement the facility will be paid in its entirety by December 2008. At June 30, 2008, the outstanding balance under this facility was \$43.4 million with a current weighted average note rate of 4.49%.

We have an uncommitted master repurchase agreement with a financial institution, effective April 2008, entered into for the purpose of financing our CRE CDO bond securities. The agreement has a term expiring in May 2010 and bears interest at pricing over LIBOR, varying on the type of asset financed. At June 30, 2008, the outstanding balance under this facility was \$40.2 million with a current weighted average note rate of 4.09%.

We had a \$100.0 million master repurchase agreement with Nomura Credit and Capital, Inc. that expired in December 2007. We exercised our right under the repurchase agreement to extend the repayment date until June

[Table of Contents](#)

2008. No further advances were permitted under the agreement. This repurchase agreement bore interest at pricing over LIBOR, varying on the type of asset financed. This facility was repaid in its entirety in February 2008.

CDOs

We completed three separate CDOs since 2005 by issuing to third party investors, tranches of investment grade collateralized debt obligations through newly-formed wholly-owned subsidiaries (the "Issuers"). The Issuers hold assets, consisting primarily of real-estate related assets and cash which serve as collateral for the CDOs. The assets pledged as collateral for the CDOs were contributed from our existing portfolio of assets. By contributing these real estate assets to the various CDOs, these transactions resulted in a decreased cost of funds relating to the corresponding CDO assets and created capacity in our existing credit facilities.

The Issuers issued tranches of investment grade floating-rate notes of approximately \$305.0 million, \$356.0 million and \$447.5 million for CDO I, CDO II and CDO III, respectively. CDO III also has a \$100.0 million revolving note which was not drawn upon at the time of issuance. The revolving note facility has a commitment fee of 0.22% per annum on the undrawn portion of the facility. The tranches were issued with floating rate coupons based on three-month LIBOR plus pricing of 0.44% — 0.77%. Proceeds from the sale of the investment grade tranches issued in CDO I, CDO II and CDO III of \$267.0 million, \$301.0 million and \$317.1 million, respectively, were used to repay higher costing outstanding debt under our repurchase agreements and notes payable. The CDOs may be replenished with substitute collateral for loans that are repaid during the first four years for CDO I and the first five years for CDO II and CDO III, subject to certain customary provisions. Thereafter, the outstanding debt balance will be reduced as loans are repaid. Proceeds from the repayment of assets which serve as collateral for the CDOs must be retained in its structure as restricted cash until such collateral can be replaced and therefore not available to fund current cash needs. If such cash is not used to replenish collateral, it could have a negative impact on our anticipated returns. Proceeds from CDO I and CDO II are distributed quarterly with approximately \$2.0 million and \$1.2 million, respectively, being paid to investors as a reduction of the CDO liability. For accounting purposes, CDOs are consolidated in our financial statements.

At June 30, 2008, the outstanding note balance under CDO I, CDO II and CDO III was \$279.3 million, \$345.6 million and \$504.7 million, respectively.

The recent turmoil in the structured finance markets, in particular the sub-prime residential loan market, has negatively impacted the credit markets generally, and, as a result, investor demand for commercial real estate collateralized debt obligations has been substantially curtailed. In recent years, we have relied to a substantial extent on CDO financings to obtain match funded financing for our investments. Until the market for commercial real estate CDOs recovers, we may be unable to utilize CDOs to finance our investments and we may need to utilize less favorable sources of financing to finance our investments on a long-term basis. There can be no assurance as to when demand for commercial real estate CDOs will return or the terms of such securities investors will demand or whether we will be able to issue CDOs to finance our investments on terms beneficial to us.

Junior Subordinated Notes

The junior subordinated notes are unsecured, have a maturity of 29 to 30 years, pay interest quarterly at a floating rate of interest based on three-month LIBOR and, absent the occurrence of special events, are not redeemable during the first five years. At June 30, 2008, the aggregate outstanding balance under these facilities was \$276.1 million with a current weighted average note rate of 7.41%.

Notes Payable

Notes payable consists of two term credit agreements, a revolving credit line, a working capital facility, a bridge loan warehousing credit agreement, a note payable and a junior loan participation. At June 30, 2008, the aggregate outstanding balance under these facilities was \$635.4 million.

In June 2007, we entered into a \$60.0 million working capital facility with Wachovia. In July 2008, the facility was extended for one year to June 2009 and was amended to decrease the amount of the facility to \$45 million from \$60 million. In addition, the amendment includes required quarterly paydowns of \$3.0 million

[Table of Contents](#)

beginning October 1, 2008 and an interest rate increase from 210 bps over Libor to 500 bps over Libor. At June 30, 2008, the aggregate outstanding balance under this facility was \$47.9 million with a current weighted average note rate of 7.57%.

In November 2007, we entered in two new credit agreements with Wachovia which replaced two of our existing repurchase agreements totaling \$757.0 million with Wachovia and an affiliate of Wachovia. The outstanding balance under these two repurchase agreements totaled approximately \$542.0 million at the time the repurchase agreements were replaced. The first credit agreement consists of a \$473.0 million term loan and a \$100.0 million revolving commitment and the second credit agreement is a \$69.0 million term loan. These two new credit agreements each provide us with a commitment period of two years with a one year extension option to November 2010, bear interest at pricing over LIBOR, and have eliminated the mark to market risk as it relates to interest rate spreads that existed under the terms of the repurchase agreements.

The \$473.0 million term loan has repayment provisions which included reducing the outstanding balance to \$425.0 million by December 31, 2007 and also requires a further reduction of the outstanding balance to \$300.0 million by December 31, 2008. The advance rates for this term facility are similar to the advance rates that existed under the previous repurchase agreements. At June 30, 2008, the outstanding balance under this facility was \$362.5 million with a current weighted average note rate of 4.99%. In July 2008, we paid down an additional \$43.4 million decreasing the outstanding balance to \$319.1 million at July 31, 2008. The \$100.0 million revolving commitment is used to finance new investments and can be increased to \$200.0 million when the term loan is paid down to \$400.0 million. The term loan was paid down to \$400.0 million on February 15, 2008. At June 30, 2008, the outstanding balance under this revolving facility was \$65.3 million with a current weighted average note rate of 5.14%.

The \$69.0 million term loan includes \$10.0 million of annual repayment provisions in quarterly installments. The advance rate on this term facility is higher than the advance rate for the collateral that was in the repurchase agreement and eliminates the mark to market risk as it relates to interest rate spreads that existed under the terms of the repurchase agreement. We have also pledged our 24% equity interest in Prime Outlets Members, LLC ("POM") as part of the agreement. In the second and third year of this term facility, we will be required to paydown this facility by an additional amount equal to distributions in excess of \$10.0 million per year received by us from our investment in POM, if any. At June 30, 2008, the outstanding balance under this facility was \$53.2 million with a current weighted average note rate of 5.03%. In connection with the POM transaction in July 2008, we agreed to pay down approximately \$11.6 million of this facility from proceeds received from this transaction, decreasing the outstanding balance to \$41.6 million at July 31, 2008. In addition, 16.7% of our 24.2% equity interest in POM was released as collateral in conjunction with this paydown.

We have a \$90.0 million bridge loan warehousing credit agreement with a fourth financial institution, effective June 2005, to provide financing for bridge loans. This agreement bears a variable rate of interest, payable monthly, based on Prime plus 0% or pricing over 1, 2, 3 or 6-month LIBOR, at our option. In October 2007, this facility was amended to extend the maturity date to October 2008 and increase the amount of available financing from \$75.0 million to \$90.0 million. We currently expect to renew this facility for one year. At June 30, 2008, the outstanding balance under this facility was \$55.7 million with a current weighted average note rate of 5.27%.

We have a \$49.5 million note payable related to the POM transaction. The note is initially secured by our 16.67% interest in POM, matures in July 2016 and bears interest at a fixed rate of 4%.

We have one junior loan participation with a total outstanding balance at June 30, 2008 of \$1.3 million. This participation borrowing has a maturity date equal to the corresponding mortgage loan and is secured by the participant's interest in the mortgage loan. Interest expense is based on a portion of the interest received from the loan.

The working capital facility, bridge loan warehousing credit agreement, term and revolving credit agreements, and the master repurchase agreements require that we pay interest monthly, based on pricing over LIBOR. The amount of our pricing over these rates varies depending upon the structure of the loan or investment financed pursuant to the specific agreement.

The working capital facility, term and revolving credit agreements, bridge loan warehousing credit agreement, and the master repurchase agreements require that we pay down borrowings under these facilities pro-

[Table of Contents](#)

rata as principal payments on our loans and investments are received. In addition, if upon maturity of a loan or investment we decide to grant the borrower an extension option, the financial institutions have the option to extend the borrowings or request payment in full on the outstanding borrowings of the loan or investment extended. The financial institutions also have the right to request immediate payment of any outstanding borrowings on any loan or investment that is at least 60 days delinquent.

Cash Flow From Operations

We continually monitor our cash position to determine the best use of funds to both maximize our return on funds and maintain an appropriate level of liquidity. Historically, in order to maximize the return on our funds, cash generated from operations has generally been used to temporarily pay down borrowings under credit facilities whose primary purpose is to fund our new loans and investments. When making distributions, we have borrowed the required funds by drawing on credit capacity available under our credit facilities. To date, all distributions have been funded in this manner. All funds borrowed to make distributions have been repaid by funds generated from operations. However, in order to maintain adequate liquidity within our credit facilities for their primary purpose of funding our new loans and investments, we may begin to accumulate cash generated from operations to make the distributions.

Restrictive Covenants

Each of the credit facilities contains various financial covenants and restrictions, including minimum net worth and debt-to-equity ratios. In addition to the financial terms and capacities described above, our credit facilities generally contain covenants that prohibit us from effecting a change in control, disposing of or encumbering assets being financed and restrict us from making any material amendment to our underwriting guidelines without approval of the lender. If we violate these covenants in any of our credit facilities, we could be required to repay all or a portion of our indebtedness before maturity at a time when we might be unable to arrange financing for such repayment on attractive terms, if at all. Violations of these covenants may result in our being unable to borrow unused amounts under our credit facilities, even if repayment of some or all borrowings is not required. We were in compliance with all financial covenants and restrictions for the periods presented with the exception of the fixed and senior fixed charge coverage ratio for one financial institution for the three months ended June 30, 2008. We are required to have a fixed charge coverage ratio of 1.50 to 1.0 and a senior fixed charge coverage ratio of 1.75 to 1.0, our ratio was 1.49 to 1.0 and 1.72 to 1.0, respectively, at the end of the second quarter. We have obtained waivers of these covenants for June 30, 2008 from this financial institution and expect to permanently amend these covenant calculations.

Contractual Commitments

As of June 30, 2008, we had the following material contractual obligations (payments in thousands):

Contractual Obligations	Payments Due by Period (1)						Total
	2008	2009	2010	2011	2012	Thereafter	
Notes payable (2)	\$ 117,790	\$ 83,908	\$ 384,190	\$ —	\$ —	\$ 49,500	\$ 635,388
Collateralized debt obligations (3)	6,360	96,493	96,493	303,470	626,833	—	1,129,649
Repurchase agreements	43,383	115,210	40,163	—	—	—	198,756
Trust preferred securities	—	—	—	—	—	276,055	276,055
Outstanding unfunded commitments (4)	42,289	43,985	11,069	7,746	1,473	986	107,548
Totals	<u>\$ 200,030</u>	<u>\$ 344,648</u>	<u>\$ 536,760</u>	<u>\$ 311,248</u>	<u>\$ 628,174</u>	<u>\$ 326,536</u>	<u>\$ 2,347,396</u>

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- (1) Represents amounts due based on contractual maturities.
 - (2) Maturity date for Wachovia term and revolving facilities includes the one year extension option.
 - (3) Comprised of \$279.3 million of CDO I debt, \$345.6 million of CDO II debt and \$504.7 million of CDO III debt with a weighted average remaining maturity of 2.02, 3.46 and 3.98 years, respectively, as of June 30, 2008.
 - (4) In accordance with certain loans and investments, we have outstanding unfunded commitments of \$107.5 million as of June 30, 2008, that we are obligated to fund as the borrowers meet certain requirements. Specific requirements include, but are not limited to, property renovations, building construction, and building conversions based on criteria met by the borrower in accordance with the loan agreements.

Management Agreement

Base Management Fees. In exchange for the services that ACM provides us pursuant to the management agreement, we pay our manager a monthly base management fee in an amount equal to:

- (1) 0.75% per annum of the first \$400 million of our operating partnership's equity (equal to the month-end value computed in accordance with GAAP of total partners' equity in our operating partnership, plus or minus any unrealized gains, losses or other items that do not affect realized net income),
- (2) 0.625% per annum of our operating partnership's equity between \$400 million and \$800 million, and
- (3) 0.50% per annum of our operating partnership's equity in excess of \$800 million.

The base management fee is not calculated based on the manager's performance or the types of assets it selects for investment on our behalf, but it is affected by the performance of these assets because it is based on the value of our operating partnership's equity. We incurred \$0.9 million and \$1.8 million in base management fees for services rendered in the three and six months ended June 30, 2008, respectively. We incurred \$0.8 million and \$1.4 million in base management fees for services rendered in the three and six months ended June 30, 2007, respectively.

Incentive Compensation. Pursuant to the management agreement, our manager is also entitled to receive incentive compensation in an amount equal to:

- (1) 25% of the amount by which:
 - (a) our operating partnership's funds from operations per operating partnership unit, adjusted for certain gains and losses, exceeds
 - (b) the product of (x) the greater of 9.5% per annum or the Ten Year U.S. Treasury Rate plus 3.5%, and (y) the weighted average of (i) \$15.00, (ii) the offering price per share of our common stock (including any shares of common stock issued upon exercise of warrants or options) in any subsequent offerings (adjusted for any prior capital dividends or distributions), and (iii) the issue price per operating partnership unit for subsequent contributions to our operating partnership, multiplied by
- (2) the weighted average of our operating partnership's outstanding operating partnership units.

For the three months ended June 30, 2008, our manager earned a total of \$8.5 million of incentive compensation and has elected to receive it partially in 417,050 shares of common stock with the remainder to be paid in cash totaling \$4.8 million, payable in August 2008. Included in the \$8.5 million of incentive compensation was \$1.2 million recorded as management fee expense and \$7.3 million recorded as deferred management fee related to the incentive management fee earned from the monetization of the POM equity kicker transaction in June 2008. For the six months ended June 30, 2008, incentive compensation totaled \$10.2 million. Included in the \$10.2 million of incentive compensation was \$2.9 million recorded as management fee expense and \$7.3 million recorded as deferred management fee related to the incentive management fee earned from the monetization of the POM equity kicker transaction in June 2008. Our manager has elected to receive these payments in the form of 472,582 shares of common stock with the remainder paid in cash totaling \$5.6 million.

[Table of Contents](#)

We pay the annual incentive compensation in four installments, each within 60 days of the end of each fiscal quarter. The calculation of each installment is based on results for the 12 months ending on the last day of the fiscal quarter for which the installment is payable. These installments of the annual incentive compensation are subject to recalculation and potential reconciliation at the end of such fiscal year. Subject to the ownership limitations in our charter, at least 25% of this incentive compensation is payable to our manager in shares of our common stock having a value equal to the average closing price per share for the last 20 days of the fiscal quarter for which the incentive compensation is being paid.

The incentive compensation is accrued as it is earned. In accordance with Issue 4(b) of EITF 96-18, "Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services," the expense incurred for incentive compensation paid in common stock is determined using the valuation method described above and the quoted market price of our common stock on the last day of each quarter. At December 31 of each year, we remeasure the incentive compensation paid to our manager in the form of common stock in accordance with Issue 4(a) of EITF 96-18 which discusses how to measure at the measurement date when certain terms are not known prior to the measurement date. Accordingly, the expense recorded for such common stock is adjusted to reflect the fair value of the common stock on the measurement date when the final calculation of the annual incentive compensation is determined. In the event that the annual incentive compensation calculated as of the measurement date is less than the four quarterly installments of the annual incentive compensation paid in advance, our manager will refund the amount of such overpayment in cash and we would record a negative incentive compensation expense in the quarter when such overpayment is determined.

Origination Fees. Our manager is entitled to 100% of the origination fees paid by borrowers under each of our bridge loan and mezzanine loans that do not exceed 1% of the loan's principal amount. We retain 100% of the origination fee that exceeds 1% of the loan's principal amount.

Term and Termination. The management agreement has an initial term of two years and is renewable automatically for an additional one year period every year thereafter, unless terminated with six months' prior written notice. If we terminate or elect not to renew the management agreement in order to manage our portfolio internally, we are required to pay a termination fee equal to the base management fee and incentive compensation for the 12-month period preceding the termination. If, without cause, we terminate or elect not to renew the management agreement for any other reason, including a change of control of us, we are required to pay a termination fee equal to two times the base management fee and incentive compensation paid for the 12-month period preceding the termination.

Related Party Transactions

Due to related party was \$7.9 million at June 30, 2008 and consisted of \$8.8 million of management fees that were due to ACM which will be remitted in August 2008, which was partially offset by \$0.9 million of escrows due from ACM which were received by us in July 2008. At December 31, 2007, due to related party was \$2.4 million and consisted of \$3.2 million of management fees that were due to ACM and remitted in February 2008, which was partially offset by \$0.8 million of extension and filing fees received by ACM which were remitted to us in January 2008.

During 2006, we originated a \$7.2 million bridge loan and a \$0.3 million preferred equity investment secured by garden-style and townhouse apartments in South Carolina. We also had a 25.0% carried profits interest in the borrowing entity. In January 2008, the borrowing entity refinanced the property through ACM's Fannie Mae program and we received \$0.3 million for our profits interest as well as full repayment of the \$0.3 million preferred equity investment and the \$7.0 million outstanding balance on the bridge loan. We retained the 25% carried profits interest.

In March 2008, ACM purchased from third party investors, investment grade CDO notes issued by certain of our subsidiaries, with an aggregate face value of \$11.5 million for \$5.0 million.

We are dependent upon our manager (ACM), with whom we have a conflict of interest, to provide services to us that are vital to our operations. Our chairman, chief executive officer and president, Mr. Ivan Kaufman, is also

[Table of Contents](#)

the chief executive officer and president of our manager, and, our chief financial officer, Mr. Paul Elenio, is the chief financial officer of our manager. In addition, Mr. Kaufman and the Kaufman entities together beneficially own approximately 91% of the outstanding membership interests of ACM and certain of our employees and directors, also hold an ownership interest in ACM. Furthermore, one of our directors also serves as the trustee of one of the Kaufman entities that holds a majority of the outstanding membership interests in ACM and co-trustee of another Kaufman entity that owns an equity interest in our manager. ACM currently holds approximately 5.0 million common shares, representing 20.1% of the voting power of its outstanding stock.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the exposure to loss resulting from changes in interest rates, foreign currency exchange rates, commodity prices, equity prices and real estate values. The primary market risks that we are exposed to are real estate risk and interest rate risk.

Market Conditions

We are subject to market changes in the debt and secondary mortgage markets. These markets are currently experiencing disruptions, which could have a short term adverse impact on our earnings and financial condition.

Current conditions in the debt markets include reduced liquidity and increased risk adjusted premiums. These conditions may increase the cost and reduce the availability of debt. We attempt to mitigate the impact of debt market disruptions by obtaining adequate debt facilities from a variety of financing sources. There can be no assurance, however, that we will be successful in these efforts, that such debt facilities will be adequate or that the cost of such debt facilities will be at similar terms.

The secondary mortgage markets are also currently experiencing disruptions resulting from reduced investor demand for collateralized debt obligations and increased investor yield requirements for these obligations. In light of these conditions, we currently expect to finance our loan and investment portfolio with our current capital and debt facilities.

Real Estate Risk

Commercial mortgage assets may be viewed as exposing an investor to greater risk of loss than residential mortgage assets since such assets are typically secured by larger loans to fewer obligors than residential mortgage assets. Multi-family and commercial property values and net operating income derived from such properties are subject to volatility and may be affected adversely by a number of factors, including, but not limited to, events such as natural disasters including hurricanes and earthquakes, acts of war and/or terrorism (such as the events of September 11, 2001) and others that may cause unanticipated and uninsured performance declines and/or losses to us or the owners and operators of the real estate securing our investment; national, regional and local economic conditions (which may be adversely affected by industry slowdowns and other factors); local real estate conditions (such as an oversupply of housing, retail, industrial, office or other commercial space); changes or continued weakness in specific industry segments; construction quality, construction delays, construction cost, age and design; demographic factors; retroactive changes to building or similar codes; and increases in operating expenses (such as energy costs). In the event net operating income decreases, a borrower may have difficulty repaying our loans, which could result in losses to us. In addition, decreases in property values reducing the value of the collateral, and a lack of liquidity in the market could reduce the potential proceeds available to a borrower to repay our loans, which could also cause us to suffer losses. Even when the net operating income is sufficient to cover the related property's debt service, there can be no assurance that this will continue to be the case in the future.

Interest Rate Risk

Interest rate risk is highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors beyond our control.

Our operating results will depend in large part on differences between the income from our loans and our borrowing costs. Most of our loans and borrowings are variable-rate instruments, based on LIBOR. The objective of this strategy is to minimize the impact of interest rate changes on our net interest income. In addition, we have various fixed rate loans in our portfolio, which are financed with variable rate LIBOR borrowings. We have entered into various interest swaps (as discussed below) to hedge our exposure to interest rate risk on our variable rate LIBOR borrowings as it relates to our fixed rate loans. Many of our loans and borrowings are subject to various interest rate floors. As a result, the impact of a change in interest rates may be different on our interest income than it is on our interest expense.

[Table of Contents](#)

Based on the loans and liabilities as of June 30, 2008, and assuming the balances of these loans and liabilities remain unchanged for the subsequent twelve months, a 1.0% increase in LIBOR would decrease our annual net income and cash flows by approximately \$3.2 million. This is primarily due to various interest rate floors that are in effect at a rate that is above a 1.0% increase in LIBOR which would limit the effect of a 1.0% increase, and increased expense on variable rate debt, partially offset by our interest rate swaps that effectively convert a portion of the variable rate LIBOR based debt, as it relates to certain fixed rate assets, to a fixed basis that is not subject to a 1.0% increase. Based on the loans and liabilities as of June 30, 2008, and assuming the balances of these loans and liabilities remain unchanged for the subsequent twelve months, a 1.0% decrease in LIBOR would increase our annual net income and cash flows by approximately \$6.0 million. This is primarily due to various interest rate floors which limit the effect of a 1.0% decrease on interest income and decreased expense on variable rate debt, partially offset by our interest rate swaps that effectively converted a portion of the variable rate LIBOR based debt, as it relates to certain fixed rate assets, to a fixed basis that is not subject to a 1.0% decrease.

Based on the loans and liabilities as of December 31, 2007, and assuming the balances of these loans and liabilities remain unchanged for the subsequent twelve months, a 1.5% increase in LIBOR would decrease our annual net income and cash flows by approximately \$1.3 million. This is primarily due to various interest rate floors that are in effect at a rate that is above a 1.5% increase in LIBOR which would limit the effect of a 1.5% increase, and increased expense on variable rate debt, partially offset by our interest rate swaps that effectively convert a portion of the variable rate LIBOR based debt, as it relates to certain fixed rate assets, to a fixed basis that is not subject to a 1.5% increase. Based on the loans and liabilities as of December 31, 2007, and assuming the balances of these loans and liabilities remain unchanged for the subsequent twelve months, a 1.5% decrease in LIBOR would increase our annual net income and cash flows by approximately \$12.5 million. This is primarily due to various interest rate floors which limit the effect of a 1.5% decrease on interest income and decreased expense on variable rate debt, partially offset by our interest rate swaps that effectively converted a portion of the variable rate LIBOR based debt, as it relates to certain fixed rate assets, to a fixed basis that is not subject to a 1.5% decrease.

In the event of a significant rising interest rate environment and/or economic downturn, defaults could increase and result in credit losses to us, which could adversely affect our liquidity and operating results. Further, such delinquencies or defaults could have an adverse effect on the spreads between interest-earning assets and interest-bearing liabilities.

We invest in securities, which are designated as held-to-maturity. These securities are adjustable rate securities that generally reset on a one or three month basis. These securities are partially financed with a master repurchase agreement that bears interest at pricing over LIBOR. Based on the securities and borrowings as of June 30, 2008 and assuming the balances of these securities and borrowings remain unchanged for the subsequent twelve months, a 1% increase in LIBOR would reduce our annual net income and cash flows by approximately \$0.4 million. A 1% decrease in LIBOR would increase our annual net income and cash flows by approximately \$0.4 million.

In connection with our CDOs described in "Management's Discussion and Analysis of Financial Condition and Results of Operations," we entered into interest rate swap agreements to hedge the exposure to the risk of changes in the difference between three-month LIBOR and one-month LIBOR interest rates. These interest rate swaps became necessary due to the investor's return being paid based on a three-month LIBOR index while the assets contributed to the CDOs are yielding interest based on a one-month LIBOR index.

We had ten of these interest rate swap agreements outstanding that have combined notional values of \$1.3 billion at both June 30, 2008 and December 31, 2007. The market value of these interest rate swaps is dependent upon existing market interest rates and swap spreads, which change over time. If there were a 50 basis point increase in forward interest rates as of June 30, 2008 and December 31, 2007, the value of these interest rate swaps would have decreased by approximately \$0.1 million for both periods. If there were a 50 basis point decrease in forward interest rates as of June 30, 2008 and December 31, 2007 the value of these interest rate swaps would have increased by approximately \$0.1 million for both periods.

We have also entered into various interest rate swap agreements in connection with the issuance of variable rate junior subordinate notes. These swaps have total notional values of \$236.5 million and \$191.5 million as of June 30, 2008 and December 31, 2007, respectively. The market value of these interest rate swaps is dependent

[Table of Contents](#)

upon existing market interest rates and swap spreads, which change over time. If there had been a 50 basis point increase in forward interest rates as of June 30, 2008 and December 31, 2007, the fair market value of these interest rate swaps would have increased by approximately \$3.6 million and \$2.9 million, respectively. If there were a 50 basis point decrease in forward interest rates as of June 30, 2008 and December 31, 2007, the fair market value of these interest rate swaps would have decreased by approximately \$3.6 million and \$3.0 million, respectively.

We also have interest rate swap agreements outstanding to hedge current and outstanding LIBOR based debt relating to certain fixed rate loans within our portfolio. We had thirty two of these interest rate swap agreements outstanding that have a combined notional value of \$662.7 million as of June 30, 2008 compared to twenty seven interest rate swap agreements outstanding with combined notional values of \$584.7 million as of December 31, 2007. The fair market value of these interest rate swaps is dependent upon existing market interest rates and swap spreads, which change over time. If there had been a 50 basis point increase in forward interest rates as of June 30, 2008 and December 31, 2007, the fair market value of these interest rate swaps would have increased by approximately \$14.3 million and \$14.9 million, respectively. If there were a 50 basis point decrease in forward interest rates as of June 30, 2008 and December 31, 2007, the fair market value of these interest rate swaps would have decreased by approximately \$14.8 million and \$15.4 million, respectively.

Our hedging transactions using derivative instruments also involve certain additional risks such as counterparty credit risk, the enforceability of hedging contracts and the risk that unanticipated and significant changes in interest rates will cause a significant loss of basis in the contract. The counterparties to our derivative arrangements are major financial institutions with high credit ratings with which we and our affiliates may also have other financial relationships. As a result, we do not anticipate that any of these counterparties will fail to meet their obligations. There can be no assurance that we will be able to adequately protect against the foregoing risks and will ultimately realize an economic benefit that exceeds the related amounts incurred in connection with engaging in such hedging strategies.

We utilize interest rate swaps to limit interest rate risk. Derivatives are used for hedging purposes rather than speculation. We do not enter into financial instruments for trading purposes.

Item 4. CONTROLS AND PROCEDURES

Our management, with the participation of our chief executive officer and chief financial officer, has evaluated the effectiveness of our “disclosure controls and procedures” (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) as of the end of the period covered by this report. Based upon such evaluation, our chief executive officer and chief financial officer have concluded that, as of the end of such period, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports we file or submit under the Exchange Act and are effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act of 1934 is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

There have not been any changes in our internal controls over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during our most recent fiscal quarter 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

Not applicable.

Item 1A. RISK FACTORS

Not applicable.

Item 2. UNREGISTERED SALE OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) During the three months ended June 30, 2008, the Company issued a total of 55,532 shares of its common stock to Arbor Commercial Mortgage, LLC (the “Manager”) pursuant to the Amended and Restated Management Agreement, dated January 19, 2005 (the “Management Agreement”), by and among the Company, the Manager, Arbor Realty Limited Partnership and Arbor Realty SR, Inc. Pursuant to the Management Agreement, the Manager is entitled to an incentive fee in certain circumstances and can elect to receive the incentive fee in shares of common stock of the Company.

The issuance and sale of the shares of common stock pursuant to the Management Agreement was not registered under the Securities Act in reliance on the exemption from registration provided by Section 4(2) thereof. These transactions did not involve any public offering of common stock, the Manager had adequate access to information about the Company, and an appropriate legend was placed on the certificates evidencing the shares of common stock issued.

Item 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The annual meeting of stockholders of the Company was held on May 21, 2008, for the purpose of considering and acting upon the following:

(1) **Election of Directors.** Three Class II directors were elected and the votes cast for or against/withheld were as follows:

Nominees	Aggregate Votes	
	For	Withheld
Ivan Kaufman	20,923,557	1,245,946
C. Michael Kojaian	21,982,808	186,695
Melvin F. Lazar	21,976,518	192,985

The continuing directors of the Company are John J. Bishar, Archie R. Dykes, Joseph Martello, Kyle A. Permut, Walter K. Horn, William Helmreich and Karen K. Edwards.

(2) **Approval of Amendment to 2003 Omnibus Stock Incentive Plan.** Amendment was approved. The votes cast for, against and abstentions were as follows:

Proposal	Aggregate Votes		
	For	Against	Abstained
Approval of Amendment to the Company's 2003 Omnibus Stock Incentive Plan, as amended and restated	12,198,593	3,501,633	71,965

(3) **Ratification of Auditors.** Ernst & Young LLP was ratified as the Company's independent registered public accounting firm for fiscal year 2008. The votes cast for, against and abstentions were as follows:

Proposal	Aggregate Votes		
	For	Against	Abstained
Ratification of Ernst & Young LLP as the Company's independent auditors for fiscal year 2008	22,050,113	88,377	31,013

(4) **Stockholder Proposal Regarding Declassification of the Board of Directors.** Proposal was not approved. The votes cast for, against and abstentions were as follows:

Proposal	Aggregate Votes		
	For	Against	Abstained
Stockholder proposal requesting that the Board of Directors of the Company take the necessary steps to eliminate the classification of terms of the Company's directors to require that all of the Company's directors stand for election annually	6,439,182	9,175,076	157,934

Item 5. OTHER INFORMATION

Not applicable.

Item 6. EXHIBITS

Exhibit Number	Description
3.1	Articles of Incorporation of Arbor Realty Trust, Inc. *
3.2	Articles of Amendment to Articles of Incorporation of Arbor Realty Trust, Inc. ▲
3.3	Articles Supplementary of Arbor Realty Trust, Inc. *
3.4	Amended and Restated Bylaws of Arbor Realty Trust, Inc. ▲ ▲
4.1	Form of Certificate for Common Stock. *
4.2	Registration Rights Agreement, dated July 1, 2003 between Arbor Realty Trust, Inc. and JMP Securities, LLC *
10.1	Amended and Restated Management Agreement, dated January 19, 2005, by and among Arbor Realty Trust, Inc., Arbor Commercial Mortgage, LLC, Arbor Realty Limited Partnership and Arbor Realty SR, Inc. †
10.2	Services Agreement, dated July 1, 2003, by and among Arbor Realty Trust, Inc., Arbor Commercial Mortgage, LLC and Arbor Realty Limited Partnership. *
10.3	Non-Competition Agreement, dated July 1, 2003, by and among Arbor Realty Trust, Inc., Arbor Realty Limited Partnership and Ivan Kaufman. *
10.4	Second Amended and Restated Agreement of Limited Partnership of Arbor Realty Limited Partnership, dated January 19, 2005, by and among Arbor Commercial Mortgage, LLC, Arbor Realty Limited Partnership, Arbor Realty LPOP, Inc. and Arbor Realty GP, Inc. †
10.5	Registration Rights Agreement, dated July 1, 2003, between Arbor Realty Trust, Inc. and Arbor Commercial Mortgage, LLC. *
10.6	Pairing Agreement, dated July 1, 2003, by and among Arbor Realty Trust, Inc., Arbor Commercial Mortgage, LLC, Arbor Realty Limited Partnership, Arbor Realty LPOP, Inc. and Arbor Realty GP, Inc. *
10.7	2003 Omnibus Stock Incentive Plan, (as amended and restated on July 29, 2004). **
10.8	Amendment No. 1 to the 2003 Omnibus Stock Incentive Plan. ††
10.9	Form of Restricted Stock Agreement. *
10.10	Benefits Participation Agreement, dated July 1, 2003, between Arbor Realty Trust, Inc. and Arbor Management, LLC. *
10.11	Form of Indemnification Agreement. *
10.12	Structured Facility Warehousing Credit and Security Agreement, dated July 1, 2003, between Arbor Realty Limited Partnership and Residential Funding Corporation. *
10.13	Amended and Restated Loan Purchase and Repurchase Agreement, dated July 12, 2004, by and among Arbor Realty Funding LLC, as seller, Wachovia Bank, National Association, as purchaser, and Arbor Realty Trust, Inc., as guarantor. ***
10.14	Master Repurchase Agreement, dated as of November 18, 2002, by and between Nomura Credit and Capital, Inc. and Arbor Commercial Mortgage, LLC. *
10.15	Revolving Credit Facility Agreement, dated as of December 7, 2004, by and between Arbor Realty Trust, Inc., Arbor Realty Limited Partnership and Watershed Administrative LLC and the lenders named therein. †
10.16	Indenture, dated January 19, 2005, by and between Arbor Realty Mortgage Securities Series 2004-1, Ltd., Arbor Realty Mortgage Securities Series 2004-1 LLC, Arbor Realty SR, Inc. and LaSalle Bank National Association. †

Table of Contents

Exhibit Number	Description
10.17	Indenture, dated January 11, 2006, by and between Arbor Realty Mortgage Securities Series 2005-1, Ltd., Arbor Realty Mortgage Securities Series 2005-1 LLC, Arbor Realty SR, Inc. and LaSalle Bank National Association. ‡
10.18	Master Repurchase Agreement, dated as of October 26, 2006, by and between Column Financial, Inc. and Arbor Realty SR, Inc. and Arbor TRS Holding Company Inc., as sellers, Arbor Realty Trust, Inc., Arbor Realty Limited Partnership, as guarantors, and Arbor Realty Mezzanine LLC. ‡‡‡
10.19	Indenture, dated January 19, 2005, by and between Arbor Realty Mortgage Securities Series 2004-1, Ltd., Arbor Realty Mortgage Securities Series 2004-1 LLC, Arbor Realty SR, Inc. and Lasalle Bank National Association. †
10.20	Note Purchase Agreement, dated January 19, 2005, by and between Arbor Realty Mortgage Securities Series 2004-1, Ltd., Arbor Realty Mortgage Securities Series 2004-1 LLC and Wachovia Capital Markets, LLC. †
10.21	Indenture, dated January 11, 2006, by and between Arbor Realty Mortgage Securities Series 2005-1, Ltd., Arbor Realty Mortgage Securities Series 2005-1 LLC, Arbor Realty SR, Inc. and Lasalle Bank National Association. ‡
10.22	Note Purchase Agreement, dated January 11, 2006, by and between Arbor Realty Mortgage Securities Series 2005-1, Ltd., Arbor Realty Mortgage Securities Series 2005-1 LLC and Wachovia Capital Markets, LLC. ‡
10.23	Master Repurchase Agreement, dated as of October 26, 2006, by and between Column Financial, Inc. and Arbor Realty SR, Inc. and Arbor TRS Holding Company Inc., as sellers, Arbor Realty Trust, Inc., Arbor Realty Limited Partnership, as guarantors, and Arbor Realty Mezzanine LLC. ‡‡‡
10.24	Indenture, dated December 14, 2006, by and between Arbor Realty Mortgage Securities Series 2006-1, Ltd., Arbor Realty Mortgage Securities Series 2006-1 LLC, Arbor Realty SR, Inc. and Wells Fargo Bank, National Association. ❖
10.25	Note Purchase and Placement Agreement, dated December 14, 2006, by and between Arbor Realty Mortgage Securities Series 2006-1, Ltd., Arbor Realty Mortgage Securities Series 2006-1 LLC and Wachovia Capital Markets, LLC and Credit Suisse Securities (USA) LLC. ❖
10.26	Note Purchase Agreement, dated December 14, 2006, by and between Arbor Realty Mortgage Securities Series 2006-1, Ltd., Arbor Realty Mortgage Securities Series 2006-1 LLC and Wells Fargo Bank, National Association. ❖
10.27	Master Repurchase Agreement, dated as of March 30, 2007, by and between Variable Funding Capital Company LLC, as purchaser, Wachovia Bank, National Association, as swingline purchaser, Wachovia Capital Markets, LLC, as deal agent, Arbor Realty Funding LLC, Arbor Realty Limited Partnership and ARSR Tahoe, LLC, as sellers, Arbor Realty Trust, Inc., Arbor Realty Limited Partnership and Arbor Realty SR, Inc., as guarantors. ❖❖
10.28	Second Amendment, dated June 18, 2008, to the Amended and Restated Management Agreement by and among Arbor Realty Trust, Inc. Arbor Commercial Mortgage, LLC, Arbor Realty Limited Partnership and Arbor Realty SR, Inc.
10.29	Amendment No. 2, dated March 20, 2008, to the Arbor Realty Trust, Inc. 2003 Omnibus Stock Incentive Plan.
10.30	Amendment No. 3, dated May 21, 2008, to the Arbor Realty Trust, Inc. 2003 Omnibus Stock Incentive Plan.
31.1	Certification of Chief Executive Officer pursuant to Exchange Act Rule 13a-14.
31.2	Certification of Chief Financial Officer pursuant to Exchange Act Rule 13a-14.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

▲ Incorporated by reference to Exhibit 1.1 of the Registrant's Current Report on Form 8-K (No. 001-32136) which was filed with the Securities and Exchange Commission on June 12, 2007.

* Incorporated by reference to the Registrant's Registration Statement on Form S-11 (Registration No. 333-110472), as amended. Such registration statement was originally filed with the Securities and Exchange Commission on November 13, 2003.

** Incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2004.

*** Incorporated by reference to the Registrant's Quarterly Report of Form 10-Q for the quarter ended September 30, 2004.

[Table of Contents](#)

- † Incorporated by reference to the Registrant's Annual Report of Form 10-K for the year ended December 31, 2004.
- ‡ Incorporated by reference to the Registrant's Annual Report of Form 10-K for the year ended December 31, 2005.
- ‡‡ Incorporated by reference to the Registrant's Quarterly Report of Form 10-Q for the quarter ended June 30, 2005.
- ‡‡‡ Incorporated by reference to the Registrant's Quarterly Report of Form 10-Q for the quarter ended September 30, 2006.
- ❖ Incorporated by reference to the Registrant's Annual Report of Form 10-K for the year ended December 31, 2007.
- ❖❖ Incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2007.

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:

ARBOR REALTY TRUST, INC.
(Registrant)

By: /s/ Ivan Kaufman
Name: Ivan Kaufman
Title: Chief Executive Officer

By: /s/ Paul Elenio
Name: Paul Elenio
Title: Chief Financial Officer

Date: August 8, 2008

**SECOND AMENDMENT TO THE AMENDED AND RESTATED
MANAGEMENT AND ADVISORY AGREEMENT**

THIS SECOND AMENDMENT TO THE AMENDED AND RESTATED MANAGEMENT AND ADVISORY AGREEMENT is made as of June 18, 2008 (the "Amendment") by and among ARBOR REALTY TRUST, INC., a Maryland corporation ("Parent REIT"), ARBOR REALTY LIMITED PARTNERSHIP, a Delaware limited partnership (the "Operating Partnership"), ARBOR REALTY SR, INC., a Maryland corporation ("Sub-REIT") and together with the Parent REIT and the Operating Partnership, the "Company", and ARBOR COMMERCIAL MORTGAGE, LLC, a New York limited liability company (together with its permitted assigns, "Manager").

WITNESSETH:

WHEREAS, Parent REIT, Sub-REIT, Manager and the Operating Partnership have entered into that certain Amended and Restated Management and Advisory Agreement, dated as of January 18, 2005 (the "Management Agreement");

WHEREAS, Parent REIT, Sub-REIT, Manager and the Operating Partnership agreed to amend the Management Agreement on February 7, 2007 in order provide that for the quarter in which proceeds were received by Parent REIT from the transaction described in such amendment (the "First Transaction"), Funds from Operations (as defined in the Management Agreement) was to be calculated assuming that the Parent REIT had recorded a book gain from the First Transaction and that at such time that Parent REIT actually records a book gain from the First Transaction, the amount of such book gain was to be deducted from the calculation of Funds from Operations for the quarter in which such book gain was recognized;

WHEREAS, Parent REIT desires to proceed with the proposed transaction described in the memorandum attached hereto as Appendix 1 (the "Second Transaction");

WHEREAS, the Parent REIT, Sub-REIT, Manager and the Operating Partnership desire to amend the Management Agreement in the manner and as more fully set forth herein; and

WHEREAS, as permitted by Section 27 of the Management Agreement, the parties hereto have consented to this Amendment in the manner and as more fully set forth herein.

NOW THEREFORE, in consideration of the mutual agreements herein set forth, the parties hereto agree as follows:

1. Amendment to Section 1(o). The definition of "Funds from Operations" is hereby deleted in its entirety and replaced with the following definition:

"Funds from Operations" has the meaning assigned by the National Association of Real Estate Investment Trusts and means net income (computed in accordance with GAAP) excluding gains (or losses) from debt restructuring and sales of property, plus depreciation and amortization on real estate assets, and after adjustments for unconsolidated partnerships and joint ventures; provided, however, that (i) for the quarter in which proceeds are received by Parent REIT from the First Transaction or the Second Transaction, as applicable, Funds from Operations will be calculated assuming that Parent REIT had recorded a book gain from the First Transaction or the Second Transaction, as applicable, (ii) at such time that Parent REIT actually records a book gain from the First Transaction or the Second Transaction, as applicable, the amount of such book gain will be deducted from the calculation of Funds from Operations for the quarter in which such book gain is recognized, and (iii) if the Second Transaction is not consummated and therefore, the Parent REIT determines that it will not actually record a book gain from the Second Transaction, the amount of book gain assumed to have been recorded when calculating Funds from Operations for the quarter in which proceeds were received by Parent REIT from the Second Transaction will be deducted from the calculation of Funds from Operations for the quarter in which such determination is made.

2. Ratification. Except as modified pursuant to this Amendment, the Management Agreement, as amended by the First Amendment thereto, dated as of February 7, 2007, is ratified and confirmed in all respects.

Capitalized terms not defined in this Amendment shall have the respective meanings set forth in the Management Agreement.

[NO FURTHER TEXT ON THIS PAGE]

IN WITNESS WHEREOF, the parties hereto have executed this Amendment as of the date first above written.

Manager:

ARBOR COMMERCIAL MORTGAGE, LLC,
a New York limited liability company

By: /s/ Paul Elenio
Name: Paul Elenio
Title: Chief Financial Officer

Parent REIT:

ARBOR REALTY TRUST, INC.,
a Maryland corporation

By: /s/ Paul Elenio
Name: Paul Elenio
Title: Chief Financial Officer

Operating Partnership:

ARBOR REALTY LIMITED PARTNERSHIP,
a Delaware limited partnership

By: Arbor Realty GPOP, Inc.,
a Delaware corporation,
its general partner

By: /s/ Paul Elenio
Name: Paul Elenio
Title: Treasurer

Sub-REIT:

ARBOR REALTY SR, INC.,
a Maryland corporation

By: /s/ Paul Elenio
Name: Paul Elenio
Title: Chief Financial Officer

Appendix 1
Memorandum

To: Board of Directors
From: Paul Elenio
Date: June 16, 2008
Re: Prime transaction

We currently own a 24.17% equity and profits interest in Prime Outlets. As previously discussed, at our board meeting on May 21, 2008, we have agreed to dispose of 16.67% of our interest in Prime Outlets for approximately \$37 million with a REIT controlled by David Lichtenstein (the key principal of Prime). Upon completion of this transaction, we will retain a 7.5% interest in Prime.

The form of the transaction is such that we will contribute our 16.67% interest in Prime in exchange for \$37 million of operating partnership units in a REIT controlled by David. The REIT will also lend us \$33 million (or 90% of the \$37 million consideration), with an eight year term, secured by our operating partnership units. The units will be redeemable at the option of the REIT for cash in five years with a provision that if they are redeemed the loan will be repaid at that time. The units will earn a preferred return and our debt will pay an interest rate that will net to a 9% return on the \$4 million that we will not receive until our units are redeemed for cash.

This structure will provide us with a tax deferral for a five year period, subject to certain carve out provisions, which allows us to retain these proceeds adding greatly to our liquidity and working capital. In order to complete this transaction, David needs to generate audited financial statements for all the properties in Prime so that our 16.67% interest can be contributed to his REIT. He estimates that this will take around six to eight months to complete. Due to this timing issue, his REIT has agreed to lend us \$33 million, on the date we sign the agreement, secured by our interest in Prime. Upon receiving the necessary audited financial statements, we will exchange our Prime interest for operating partnership units in his REIT and those units will then be the collateral for our loan. If he is unable to close this transaction in the six to eight month time frame, he will be obligated to pay liquidating damages of approximately \$4 million and our loan will remain outstanding for its eight year term and we will also retain our 16.67% interest in Prime. Upon the completion of this transaction ART would have received approximately \$195 million of undistributed cash proceeds from the monetization of equity kickers through tax deferred structures.

We anticipate receiving an opinion of "more likely than not" from Cooley Godward Kronish LLP, deal counsel on this transaction.

After discussing this transaction with our auditors, the accounting treatment for this transaction will result in us recording, in our second quarter 2008 financial statements, approximately \$33 million of cash and debt related to the proceeds received from the loan secured by the Company's 16.67% interest in Prime Outlets. Upon closing this transaction, the Company will

record an investment of approximately \$37 million for the preferred and common operating partnership units, income of approximately \$33 million, a deferred gain of approximately \$4 million and a management fee expense of approximately \$8 million.

Since it will take six to eight months to close this transaction, the Company will not record income on the initial receipt of cash and under the terms of the management agreement the manager, Arbor Commercial Mortgage, LLC (“ACM”), will not receive its incentive management fee payment until the transaction closes. Management is of the opinion that this is only the case as a result of us structuring this deal in a tax efficient manner which provides the maximum benefit to ART by allowing us to retain a significant amount of capital and defer the tax liability related to this transaction and prior deferred taxes related to this investment for five years. We estimate the management fee related to the \$33 million cash proceeds received upon signing will be approximately \$8 million. We are therefore requesting that the Board grant a waiver to authorize advancing the manager the incentive fee associated with this transaction contingent on the fact that the transaction closes in six to eight months and the gain is ultimately recorded. If the transaction does not close and no gain is recorded, the manager will refund the management fee in full at that time. We have received confirmation from Ernst & Young that the proper accounting treatment would be to record the payment to ACM as a prepaid expense. It is also important to note that ACM will not be receiving any incentive fee payment on the \$4 million that ART will not receive until the operating partnership units are redeemed for cash which is estimated to be in five years.

If the board approves the payment of the management fee, we will circulate a draft waiver to the Management Agreement and a consent resolution for your approval and signature.

**Amendment No. 2 to the
Arbor Realty Trust, Inc. 2003 Omnibus Stock Incentive Plan**

Pursuant to the approval of the Board of Directors of Arbor Realty Trust, Inc. (the "Company") on March 20, 2008, the first sentence of Section 3 of the Arbor Realty Trust, Inc. 2003 Omnibus Stock Incentive Plan (as Amended and Restated on July 29, 2004), as further amended by Amendment No. 1 thereto adopted on May 25, 2005, is hereby amended to state as follows:

"The total number of shares of Common Stock reserved and available for issuance under the Plan shall be 735,000 shares."

Dated: March 20, 2008

ARBOR REALTY TRUST, INC.

By: /s/ Paul Elenio

Name: Paul Elenio

Title: Chief Financial Officer

**Amendment No. 3 to the
Arbor Realty Trust, Inc. 2003 Omnibus Stock Incentive Plan**

Pursuant to the approval of the Board of Directors of Arbor Realty Trust, Inc. (the "Company") on April 8, 2008 and the Company's stockholders on May 21, 2008, the first sentence of Section 3 of the Arbor Realty Trust, Inc. 2003 Omnibus Stock Incentive Plan (as Amended and Restated on July 29, 2004), as further amended by Amendment No. 1 thereto adopted on May 25, 2005 and Amendment No. 2 thereto adopted on March 20, 2008, is hereby amended to state as follows:

"The total number of shares of Common Stock reserved and available for issuance under the Plan shall be 1,135,000 shares."

Dated: May 21, 2008

ARBOR REALTY TRUST, INC.

By: /s/ Paul Elenio
Name: Paul Elenio
Title: Chief Financial Officer

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Ivan Kaufman, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Arbor Realty Trust, Inc.;
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 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 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: August 8, 2008

By: /s/ Ivan Kaufman
 Name: Ivan Kaufman
 Title: Chief Executive Officer

CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, Paul Elenio, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Arbor Realty Trust, Inc.;
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 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 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: August 8, 2008

By: /s/ Paul Elenio
Name: Paul Elenio
Title: Chief Financial Officer

**CERTIFICATION OF CEO 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 on Form 10-Q of Arbor Realty Trust, Inc. (the "Company") for the quarterly period ended June 30, 2008 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Ivan Kaufman, as Chief Executive Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of his knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

By: /s/ Ivan Kaufman

Name: Ivan Kaufman
Title: Chief Executive Officer

Date: August 8, 2008

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

**CERTIFICATION OF CFO 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 on Form 10-Q of Arbor Realty Trust, Inc. (the "Company") for the quarterly period ended June 30, 2008 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Paul Elenio, as Chief Financial Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of his knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

By: /s/ Paul Elenio

Name: Paul Elenio
Title: Chief Financial Officer

Date: August 8, 2008

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.