Resource Capital Corp.
Form 10-Q
November 13, 2006

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2006

OR

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

For the transition period from _________ to __________

Commission file number: 1-32733

RESOURCE CAPITAL CORP.
(Exact name of registrant as specified in its charter)

Maryland	**20-2287134**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

712 5th Avenue, 10th Floor	
New York, NY	**10019**
(Address of principal executive offices)	(Zip Code)

212-506-3870
(Registrant's telephone number, including area code)

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. x Yes ¨ No

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

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ¨

Yes x No

The number of outstanding shares of the registrant's common stock on November 1, 2006 was 17,821,434 shares.

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
INDEX TO QUARTERLY REPORT
ON FORM 10-Q

Index

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share data)

	September 30, 2006 (Unaudited)	December 31, 2005
ASSETS		
Cash and cash equivalents	$ 13,505	$ 17,729
Restricted cash	29,054	23,592
Receivables on investment securities sold	753,195	–
Due from broker	–	525
Available-for-sale securities, pledged as collateral, at fair value	395,884	1,362,392
Available-for-sale securities, at fair value	–	28,285
Loans	1,054,602	569,873
Direct financing leases and notes, net of unearned income	91,909	23,317
Investments in unconsolidated trusts	1,548	–
Derivatives, at fair value	–	3,006
Interest receivable	11,369	9,337
Accounts receivable	503	183
Principal paydown receivables	14,668	5,805
Other assets	3,142	1,503
Total assets	$ 2,369,379	$ 2,045,547
LIABILITIES		
Repurchase agreements, including accrued interest of $1,012 and $2,104	$ 770,167	$ 1,068,277
Collateralized debt obligations (“CDOs”) (net of debt issuance costs of $18,730 and $10,093)	1,206,751	687,407
Warehouse agreement	–	62,961
Secured term facility	87,080	–
Unsecured revolving credit facility	–	15,000
Distribution payable	6,594	5,646
Accrued interest expense	11,357	9,514
Unsecured junior subordinated debentures held by unconsolidated trusts that issued trust preferred securities	51,548	–
Management and incentive fee payable – related party	614	896
Derivatives, at fair value	3,094	–
Security deposits	868	–
Accounts payable and accrued liabilities	1,319	513
Total liabilities	2,139,392	1,850,214
STOCKHOLDERS’ EQUITY		
Preferred stock, par value $0.001: 100,000,000 shares authorized; no shares issued and outstanding	-	-
Common stock, par value $0.001: 500,000,000 shares authorized; 17,821,434 and 15,682,334 shares issued and outstanding (including 234,224 and 349,000 restricted shares)	18	16

Additional paid-in capital		247,934		220,161
Deferred equity compensation		(1,364)		(2,684)
Accumulated other comprehensive loss		(3,951)		(19,581)
Distributions in excess of earnings		(12,650)		(2,579)
Total stockholders' equity		229,987		195,333
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$	2,369,379	$	2,045,547

See accompanying notes to consolidated financial statements

3

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except share and per share data)
(Unaudited)

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Period from March 8, 2005 (Date Operations Commenced) to September 30, 2005
REVENUES				
Net interest income:				
Interest income from securities available-for-sale	$ 16,248	$ 16,248	$ 48,673	$ 26,741
Interest income from loans	19,905	4,864	46,625	6,322
Interest income – other	2,995	484	8,179	1,627
Total interest income	39,148	21,596	103,477	34,690
Interest expense	30,855	15,595	78,576	23,736
Net interest income	8,293	6,001	24,901	10,954
OTHER (LOSS) REVENUE				
Net realized (losses) gains on investments	(8,314)	192	(8,853)	178
Other income	384	–	391	–
Total other (loss) revenue	(7,930)	192	(8,462)	178
EXPENSES				
Management fees – related party	917	822	3,147	1,839
Equity compensation – related party	798	836	1,620	1,873
Professional services	480	222	1,266	344
Insurance	126	122	372	273
General and administrative	443	415	1,220	795
Total expenses	2,764	2,417	7,625	5,124
NET (LOSS) INCOME	$ (2,401)	$ 3,776	$ 8,814	$ 6,008
NET (LOSS) INCOME PER SHARE - BASIC	$ (0.14)	$ 0.25	$ 0.51	$ 0.39
NET (LOSS) INCOME PER SHARE - DILUTED	$ (0.14)	$ 0.24	$ 0.51	$ 0.39
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING – BASIC	17,585,171	15,333,334	17,261,091	15,333,334
	17,585,171	15,458,133	17,388,566	15,458,133

WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING – DILUTED				
DIVIDENDS DECLARED PER SHARE	$ 0.37	$ 0.20	$ 1.06	$ 0.20

See accompanying notes to consolidated financial statements

4

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
NINE MONTHS ENDED SEPTEMBER 30, 2006
(in thousands, except share data)
(Unaudited)

	Common Shares	Stock Amount	Additional Paid-In Capital	Deferred Equity Compensation	Accumulated Other Comprehensive Loss	Retained Earnings	Distributions in Excess of Earnings	Comprehensive Income	Total Stockholders' Equity
Balance, January 1, 2006	15,682,334	$ 16	$ 220,161	$ (2,684)	$ (19,581)	$ –	$ (2,579)	$ (19,581)	$ 195,333
Net proceeds from common stock offerings	2,120,800	2	29,663						29,665
Offering costs			(2,384)						(2,384)
Stock based compensation	18,300		254	(60)					194
Stock based compensation, fair value adjustment			240	(240)					–
Amortization of stock based compensation				1,620					1,620
Net income						8,814		8,814	8,814
Available-for-sale securities, fair value adjustment					21,847			21,847	21,847
Designated derivatives, fair value adjustment					(6,217)			(6,217)	(6,217)
Distributions on common stock						(8,814)	(10,071)		(18,885)
Comprehensive income								$ 4,863	
Balance, September 30, 2006	17,821,434	$ 18	$ 247,934	$ (1,364)	$ (3,951)	$ –	$ (12,650)		$ 229,987

See accompanying notes to consolidated financial statements

5

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

	Nine Months Ended September 30, 2006	Period from March 8, 2005 (Date Operations Commenced) to September 30, 2005
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 8,814	$ 6,008
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	250	–
Amortization of discount on investments and notes	(362)	(259)
Amortization of debt issuance costs	1,094	183
Amortization of stock-based compensation	1,620	1,873
Non-cash incentive compensation to the manager	108	–
Net realized gain on derivative instruments	(3,453)	–
Net realized loss (gain) on investments	11,427	(178)
Changes in operating assets and liabilities:		
Increase in restricted cash	(5,463)	–
Decrease (increase) in due from broker	525	(6,635)
Increase in interest receivable, net of purchased interest	(2,102)	(7,968)
Increase in accounts receivable	(368)	–
Decrease (increase) in principal paydown receivables	2,801	(4,701)
Increase in other assets	(1,873)	(1,166)
Increase in accrued interest expense	750	11,587
(Decrease) increase in management and incentive fee payable	(196)	549
Increase in security deposits	868	–
Increase in accounts payable and accrued liabilities	844	613
Net cash provided by (used in) operating activities	15,284	(94)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of securities available-for-sale	(8,939)	(1,538,995)
Principal payments received on securities available-for-sale	117,402	79,230
Proceeds from sale of securities available-for-sale	131,577	5,483
Purchase of loans	(743,113)	(470,151)
Principal payments received on loans	154,764	9,630
Proceeds from sale of loans	103,793	58,079
Purchase of direct financing leases and notes	(97,524)	(25,097)
Proceeds from and payments received on direct financing leases and notes	29,509	–
Purchase of property and equipment	(6)	–
Net cash used in investing activities	(312,537)	(1,881,821)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net proceeds from issuances of common stock (net of offering costs of $2,384 and $566)	27,281	214,784
Proceeds from borrowings:		

Repurchase agreements	7,060,816	5,494,638
Collateralized debt obligations	527,980	689,500
Warehouse agreements	159,616	572,927
Secured term facility	109,333	–
Unsecured credit facility	21,000	–
Payments on borrowings:		
Repurchase agreements	(7,357,834)	(4,436,030)
Warehouse agreements	(222,577)	(537,672)
Secured term facility	(22,253)	–
Unsecured revolving credit facility	(36,000)	–
Proceeds from issuance of unsecured junior subordinated debentures to subsidiary trusts issuing preferred securities	50,000	–
Settlement of derivative instruments	3,335	–
Payment of debt issuance costs	(9,731)	(10,554)
Distributions paid on common stock	(17,937)	(3,136)
Net cash provided by financing activities	293,029	1,984,457
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(4,224)	102,542
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	17,729	–
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 13,505	$ 102,542

6

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS – (Continued)
(in thousands)
(Unaudited)

	Nine Months Ended September 30, 2006	Period from March 8, 2005 (Date Operations Commenced) to September 30, 2005
NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Distributions on common stock declared but not paid	$ 6,594	$ –
Unsettled security sales – receivables on investment securities sold	$ 753,195	$ –
Unsettled security sales - principal paydown receivables	$ 14,481	$ –
Unsettled security purchases - due to broker	$ –	$ 3,000
Issuance of restricted stock	$ –	$ 5,393
SUPPLEMENTAL DISCLOSURE:		
Interest expense paid in cash	$ 107,195	$ 17,960

See accompanying notes to consolidated financial statements

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006
(Unaudited)

NOTE 1 - ORGANIZATION AND BASIS OF QUARTERLY PRESENTATION

Resource Capital Corp. and subsidiaries (the ‘‘Company’’) was incorporated in Maryland on January 31, 2005 and commenced its operations on March 8, 2005 upon receipt of the net proceeds from a private placement of shares of its common stock. The Company’s principal business activity is to purchase and manage a diversified portfolio of commercial real estate-related assets and commercial finance assets. The Company’s investment activities are managed by Resource Capital Manager, Inc. (‘‘Manager’’) pursuant to a management agreement (‘‘Management Agreement’’). The Manager is a wholly owned indirect subsidiary of Resource America, Inc. (“RAI”) (Nasdaq: REXI).

The consolidated financial statements and the information and tables contained in the notes to the consolidated financial statements are unaudited. However, in the opinion of management, these interim financial statements include all adjustments necessary to fairly present the results of the interim periods presented. The unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in the Company’s Annual Report on Form 10-K for the period ended December 31, 2005. The results of operations for the three and nine months ended September 30, 2006 may not necessarily be indicative of the results of operations for the full year ending December 31, 2006.

Certain reclassifications have been made to the 2005 consolidated financial statements to conform to the 2006 presentation.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Income Taxes

For financial reporting purposes, current and deferred taxes are provided for on the portion of earnings recognized by the Company with respect to its interest in Resource TRS, Inc. (“Resource TRS”), a domestic taxable real estate investment trust (“REIT”) subsidiary, because it is taxed as a regular subchapter C corporation under the provisions of the Internal Revenue Code of 1986, as amended. As of September 30, 2006, Resource TRS did not have any taxable income.

Apidos CDO I and Apidos CDO III, the Company’s foreign taxable REIT subsidiaries, are organized as exempted companies incorporated with limited liability under the laws of the Cayman Islands, and are generally exempt from federal and state income tax at the corporate level because their activities in the United States are limited to trading in stock and securities for their own account. Therefore, despite their status as taxable REIT subsidiaries, they generally will not be subject to corporate tax on their earnings and no provision for income taxes is required; however, because they are “controlled foreign corporations,” the Company will generally be required to include Apidos CDO I’s and Apidos CDO III’s current taxable income in its calculation of REIT taxable income.

Allowance and Provision for Loan Losses

At September 30, 2006, all of the Company’s loans are current with respect to the scheduled payments of principal and interest. In reviewing the portfolio of loans and the observable secondary market prices, the Company did not identify any loans that exhibit characteristics indicating that impairment has occurred. Accordingly, as of September 30, 2006, the Company had not recorded an allowance for loan losses.

8

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Stock Based Compensation

The Company has adopted Statement of Financial Accounting Standards (“SFAS”) No. 123(R), “Share Based Payment,” as of January 1, 2006. Issuances of restricted stock and options are accounted for using the fair value based methodology prescribed by SFAS No. 123(R) whereby the fair value of the award is measured on the grant date and recorded in stockholders’ equity through an increase to additional paid-in capital and an offsetting entry to deferred equity compensation (a contra-equity account). For issuances to the Company’s Manager, the unvested stock and options are adjusted quarterly to reflect changes in fair value as performance under the agreement is completed. For issuance to the Company’s four non-employee directors, the amount is not remeasured under the fair value-based method. The deferred compensation for each of these issuances is amortized over the service period and included in equity compensation expense (see Note 8).

Variable Interest Entities

During July 2005, the Company entered into warehouse and master participation agreements with an affiliate of Citigroup Global Markets Inc. (“Citigroup”) providing that Citigroup will fund the purchase of loans by Apidos CDO III. On May 9, 2006, the Company terminated its Apidos CDO III warehouse agreement with Citigroup upon the closing of the CDO. The warehouse funding liability was replaced with the issuance of long-term debt by Apidos CDO III. The Company owns 100% of the equity issued by Apidos CDO III and is deemed to be the primary beneficiary. As a result, the Company consolidated Apidos CDO III at September 30, 2006.

Accounting for Certain Mortgage-Backed Securities and Related Repurchase Agreements

In certain circumstances, the Company has purchased debt investments from a counterparty and subsequently financed the acquisition of those debt investments through repurchase agreements with the same counterparty. The Company currently records the acquisition of the debt investments as assets and the related repurchase agreements as financing liabilities gross on the consolidated balance sheets. Interest income earned on the debt investments and interest expense incurred on the repurchase obligations are reported gross on the consolidated statements of operations. However, under a certain technical interpretation of SFAS 140, “Accounting for Transfers and Servicing of Financial Assets,” such transactions may not qualify as a purchase. Management of the Company believes, and it is industry practice, that it is accounting for these transactions in an appropriate manner. However, the result of this technical interpretation would prevent the Company from presenting the debt investments and repurchase agreements and the related interest income and interest expense on a gross basis on the Company’s consolidated financial statements. Instead, the Company would present the net investment in these transactions with the counterparty as a derivative with the corresponding change in fair value of the derivative being recorded through earnings. The value of the derivative would reflect changes in the value of the underlying debt investments and changes in the value of the underlying credit provided by the counterparty. As of September 30, 2006, the Company had no transactions in mortgage-backed securities where debt instruments were financed with the same counterparty.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

Interest Rate Risk

The primary market risk to the Company is interest rate risk. Interest rates are highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors beyond the Company’s control. Changes in the general level of interest rates can affect net interest income, which is the difference between the interest income earned on interest-earning assets and the interest expense incurred in connection with the interest-bearing liabilities, by affecting the spread between the interest-earning assets and interest-bearing liabilities. Changes in the level of interest rates also can affect the value of the Company’s interest-earning assets and the Company’s ability to realize gains from the sale of these assets. A decline in the value of the Company’s interest-earning assets pledged as collateral for borrowings under repurchase agreements could result in the counterparties demanding additional collateral pledges or liquidation of some of the existing collateral to reduce borrowing levels.

The Company seeks to manage the extent to which net income changes as a function of changes in interest rates by matching adjustable-rate assets with variable-rate borrowings. During periods of changing interest rates, interest rate mismatches could negatively impact the Company’s consolidated financial condition, consolidated results of operations and consolidated cash flows. In addition, the Company mitigates the potential impact on net income of periodic and lifetime coupon adjustment restrictions in its investment portfolio by entering into interest rate hedging agreements such as interest rate caps and interest rate swaps.

Changes in interest rates may also have an effect on the rate of mortgage principal prepayments and, as a result, prepayments on mortgage-backed securities in the Company’s investment portfolio. The Company seeks to mitigate the effect of changes in the mortgage principal repayment rate by balancing assets purchased at a premium with assets purchased at a discount. At September 30, 2006, the aggregate discount exceeded the aggregate premium on the Company’s mortgage-backed securities by approximately $3.3 million. At December 31, 2005, the aggregate discount exceeded the aggregate premium on the Company’s mortgage-backed securities by approximately $2.8 million.

Recent Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (“FASB”) issued Interpretation (“FIN 48”), “Accounting for Uncertainty in Income Taxes - An Interpretation of SFAS 109.” FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB 109, “Accounting for Income Taxes.” FIN 48 also prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The new FASB standard also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The provisions of FIN 48 are effective for fiscal years beginning after December 15, 2006. The Company is currently determining the effect, if any, the adoption of FIN 48 will have on its financial statements.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157 (“FAS 157”) “Fair Value Measurements”. FAS 157 clarifies the definition of fair value, establishes a framework for measuring fair value in GAAP and expands the disclosure of fair value measurements. This statement is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company is currently determining the effect, if any, the adoption of FAS 157 will have on its financial statements.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

Recent Accounting Pronouncements – (Continued)

In September 2006, the Securities and Exchange Commission staff issued Staff Accounting Bulletin No. 108, “Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements” (“SAB 108”). SAB 108 provides guidance for how errors should be evaluated to assess materiality from a quantitative perspective. SAB 108 permits companies to initially apply its provisions by either restating prior financial statements or recording the cumulative effect of initially applying the approach as adjustments to the carrying values of assets and liabilities as of January 1, 2006 with an offsetting adjustment to retained earnings. SAB 108 is required to be adopted for the fiscal years ending after November 30, 2006 and is not expected to have a material effect on the Company’s financial statements.

NOTE 3 - RESTRICTED CASH

Restricted cash consists of $24.8 million of principal and interest payments collected on investments held in four CDO trusts, a $1.5 million credit facility reserve used to fund future investments that will be acquired by the Company’s two bank loan CDO trusts and a $1.2 million expense reserve used to cover CDOs’ operating expenses. The remaining $1.6 million consists of an interest reserve and security deposits held in connection with the Company’s equipment lease and loan portfolio.

NOTE 4 - SECURITIES AVAILABLE-FOR-SALE

On September 27, 2006, the Company entered into an agreement to sell its remaining agency residential mortgage-backed securities (“RMBS”) for gross proceeds totaling $753.2 million, realizing a loss of $10.9 million. The proceeds from this sale were used to repay related debt of $716.5 million on October 2, 2006. The balance of the proceeds will be subsequently received in October and November 2006. Principal repayment receivables of $14.5 million relating to the agency RMBS portfolio sold have been reflected in principal paydown receivables in the Company’s consolidated balance sheets.

The following tables summarize the Company's mortgage-backed securities, other asset-backed securities and private equity investments, including those pledged as collateral and classified as available-for-sale, which are carried at fair value (in thousands):

September 30, 2006 (Unaudited):	**Amortized Cost**	**Unrealize Gains**	**Unrealized Losses**	**Estimated Fair Value**
ABS-RMBS	$ 346,988	$ 1,813	$ (1,733)	$ 347,068
Commercial mortgage-backed	27,954	4	(570)	27,388
Other asset-backed	21,452	113	(137)	21,428
Total	$ 396,394	$ 1,930	$ (2,440)	$ 395,884 (1)
December 31, 2005:				
Agency RMBS	$ 1,014,575	$ 13	$ (12,918)	$ 1,001,670
ABS-RMBS	346,460	370	(9,085)	337,745
Commercial mortgage-backed	27,970	1	(608)	27,363

Other asset-backed	22,045	24	(124)	21,945
Private equity	1,984	–	(30)	1,954
Total	$ 1,413,034	$ 408	$ (22,765)	$ 1,390,677 (1)

(1) As of September 30, 2006, all securities were pledged as collateral. As of December 31, 2005, all securities, other than $26.3 million in agency RMBS and $2.0 million in private equity investments, were pledged as collateral.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

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

The following tables summarize the estimated maturities of the Company's mortgage-backed securities, other asset-backed securities and private equity investments according to their estimated weighted average life classifications (in thousands, except percentages):

Weighted Average Life	Estimated Fair Value	Amortized Cost	Weighted average Coupon
September 30, 2006 (Unaudited):			
Less than one year	$ 3,971	$ 3,967	6.66%
Greater than one year and less than five years	344,999	345,110	6.88%
Greater than five years	46,914	47,317	6.19%
Total	$ 395,884	$ 396,394	6.79%
December 31, 2005:			
Less than one year	$ –	$ –	–%
Greater than one year and less than five years	1,355,910	1,377,537	4.91%
Greater than five years	34,767	35,497	5.60%
Total	$ 1,390,677	$ 1,413,034	4.92%

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

	Less than 12 Months		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
September 30, 2006 (Unaudited):				
ABS-RMBS	$ 74,533	$ (798)	$ 153,692	$ (1,733)
Commercial mortgage-backed	19,093	(568)	26,968	(570)
Other asset-backed	2,999	(137)	2,999	(137)
Total temporarily impaired securities	$ 96,625	$ (1,503)	$ 183,659	$ (2,440)
December 31, 2005:				
Agency RMBS	$ 978,570	$ (12,918)	$ 978,570	$ (12,918)
ABS-RMBS	294,359	(9,085)	294,359	(9,085)
Commercial mortgage-backed	26,905	(608)	26,905	(608)
Other asset-backed	12,944	(124)	12,944	(124)
Private equity	1,954	(30)	1,954	(30)
Total temporarily impaired securities	$ 1,314,732	$ (22,765)	$ 1,314,732	$ (22,765)

The temporary impairment of the available-for-sale securities results from the estimated fair value of the securities falling below their amortized cost basis and is solely attributed to changes in interest rates. As of September 30, 2006 and December 31, 2005, respectively, none of the securities held by the Company had been downgraded by a credit rating agency since their purchase. The Company intends and has the ability to hold the securities until the estimated fair value of the securities held is recovered, which may be maturity if necessary. As such, the Company does not believe any of the securities held are other-than-temporarily impaired at September 30, 2006 and December 31, 2005, respectively.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 5 - LOANS

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

Loan Description	Principal	Unamortized (Discount) Premium	Net Amortized Cost
September 30, 2006 (Unaudited):			
Bank loans	$ 613,979	$ 968	$ 614,947
Commercial real estate loans:			
Whole loans	76,440	(619)	75,821
A notes	42,500	17	42,517
B notes	162,280	(109)	162,171
Mezzanine loans	164,750	(5,604)	159,146
Total	$ 1,059,949	$ (5,347)	$ 1,054,602
December 31, 2005:			
Bank loans	$ 397,869	$ 916	$ 398,785
Commercial real estate loans:			
B notes	121,671	–	121,671
Mezzanine loans	49,417	–	49,417
Total	$ 568,957	$ 916	$ 569,873

At September 30, 2006, the Company's bank loan portfolio consisted of $614.7 million of floating rate loans, which bear interest between London Interbank Offered Rate ("LIBOR") plus 1.38% and LIBOR plus 7.50% with maturity dates ranging from March 2007 to August 2022, and a $249,000 fixed rate loan, which bears interest at 6.25% with a maturity date of September 2015.

At December 31, 2005, the Company's bank loan portfolio consisted of $398.5 million of floating rate loans, which bear interest between LIBOR plus 1.00% and LIBOR plus 7.00% with maturity dates ranging from April 2006 to October 2020, and a $249,000 fixed rate loan, which bears interest at 6.25% with a maturity date of September 2015.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 5 - LOANS – (Continued)

The following is a summary of the loans in the Company's commercial real estate loan portfolio at the dates indicated (in thousands):

Description	Quantity		Amortized Cost	Interest Rates	Maturity Dates
September 30, 2006 (Unaudited):					
Whole loans, floating rate	4	$	75,821	LIBOR plus 2.50% to LIBOR plus 3.60%	August 2007 to September 2008
A notes, floating rate	2		42,517	LIBOR plus 1.25% to LIBOR plus 1.35%	January 2008 to April 2008
B notes, floating rate	8		120,251	LIBOR plus 1.90% to LIBOR plus 6.25%	January 2007 to April 2008
B notes, fixed rate	2		41,920	7.18% to 8.68%	April 2016 to July 2016
Mezzanine loans, floating rate	6		75,476	LIBOR plus 2.25% to LIBOR plus 4.50%	August 2007 to July 2008
Mezzanine loan, floating rate	1		6,523	10 year Treasury rate plus 6.64%	January 2016
Mezzanine loans, fixed rate	7		77,147	5.78% to 9.50%	October 2009 to September 2016
Total	30	$	439,655		
December 31, 2005:					
B notes, floating rate	7	$	121,671	LIBOR plus 2.15% to LIBOR plus 6.25%	January 2007 to April 2008
Mezzanine loans, floating rate	4		44,405	LIBOR plus 2.25% to LIBOR plus 4.50%	August 2007 to July 2008
Mezzanine loan, fixed rate	1		5,012	9.50%	May 2010
Total	12	$	171,088		

As of September 30, 2006 and December 31, 2005, the Company had not recorded an allowance for loan losses. At September 30, 2006 and December 31, 2005, all of the Company's loans were current with respect to the scheduled payments of principal and interest. In reviewing the portfolio of loans and secondary market prices, the Company did not identify any loans with characteristics indicating that impairment had occurred.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 6 -DIRECT FINANCING LEASES AND NOTES

The Company's direct financing leases have initial lease terms of 73 months and 54 months, as of September 30, 2006 and December 31, 2005, respectively. The interest rates on notes receivable range from 6% to 13% and from 8% to 9%, as of September 30, 2006 and December 31, 2005, respectively. Investments in direct financing leases and notes, net of unearned income, were as follows (in thousands):

	September 30, 2006 (Unaudited)	December 31, 2005
Direct financing leases, net of unearned income	$ 33,197	$ 18,141
Notes receivable	58,712	5,176
Total	$ 91,909	$ 23,317

The components of the net investment in direct financing leases are as follows (in thousands):

	September 30, 2006 (Unaudited)	December 31, 2005
Total future minimum lease payments	$ 39,583	$ 21,370
Unearned income	(6,386)	(3,229)
Total	$ 33,197	$ 18,141

The future minimum lease payments expected to be received on non-cancelable direct financing leases and notes were as follows (in thousands):

Years Ending September 30, (Unaudited)	Direct Financing Leases	Notes	Total
2007	$ 11,695	$ 10,299	$ 21,994
2008	10,794	10,599	21,393
2009	6,719	9,782	16,501
2010	5,714	8,035	13,749
2011	2,898	6,073	8,971
Thereafter	1,763	13,924	15,687
	$ 39,583	$ 58,712	$ 98,295

NOTE 7 - BORROWINGS

The Company finances the acquisition of its investments, including securities available-for-sale, loans and equipment leases and notes, primarily through the use of secured and unsecured borrowings in the form of CDOs, repurchase agreements, a secured term facility, warehouse facilities, trust preferred securities issuances and other secured and unsecured borrowings.

15

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 7 - BORROWINGS – (Continued)

Certain information with respect to the Company's borrowings at September 30, 2006 and December 31, 2005 is summarized in the following table (dollars in thousands):

		Outstanding Borrowings	Weighted Average Borrowing Rate	Weighted Average Remaining Maturity		Value of Collateral
September 30, 2006 (Unaudited):						
Repurchase Agreements	$	770,167	5.45%	3 days	$	818,084
RREF CDO 2006-1 Senior Notes (1)		259,850	6.15%	39.9 years		339,825
Ischus CDO II Senior Notes (2)		371,014	5.62%	33.9 years		395,884
Apidos CDO I Senior Notes (3)		317,226	5.94%	10.8 years		338,184
Apidos CDO III Senior Notes (4)		258,661	5.76%	13.7 years		275,701
Secured Term Facility		87,080	6.34%	3.5 years		91,909
Unsecured Revolving Credit Facility		–	N/A	2.3 years		–
Unsecured Junior Subordinated Debentures (5)		51,548	9.39%	29.9 years		–
Total	$	2,115,546	5.81%		$	2,259,587
December 31, 2005:						
Repurchase Agreements	$	1,068,277	4.48%	17 days	$	1,146,711
Ischus CDO II Senior Notes (2)		370,569	4.80%	34.6 years		387,053
Apidos CDO I Senior Notes (3)		316,838	4.42%	11.6 years		335,831
Apidos CDO III - Warehouse Facility (4)		62,961	4.29%	90 days		62,954
Unsecured Revolving Credit Facility		15,000	6.37%	3.0 years		45,107
Total	$	1,833,645	4.54%		$	1,977,656

---

(1) Amount represents principal outstanding of $265.5 million less unamortized issuance costs of $5.6 million as of September 30, 2006. This CDO transaction closed in August 2006.

(2) Amount represents principal outstanding of $376.0 million less unamortized issuance costs of $5.0 million and $5.4 million as of September 30, 2006 and December 31, 2005, respectively.

(3) Amount represents principal outstanding of $321.5 million less unamortized issuance costs of $4.3 million and $4.7 million as of September 30, 2006 and December 31, 2005, respectively.

(4) Amount represents principal outstanding of $262.5 million less unamortized issuance costs of $3.8 million as of September 30, 2006. This CDO transaction closed in May 2006.

(5) Amount represents junior subordinated debentures issued to Resource Capital Trust I and RCC Trust II in connection with each respective trust's issuance of trust preferred securities in May 2006 and September 2006, respectively.

16

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 7 - BORROWINGS – (Continued)

The Company had repurchase agreements with the following counterparties at the dates indicated (dollars in thousands):

		Amount at Risk (1)	Weighted Average Maturity in Days	Weighted Average Interest Rate
September 30, 2006 (Unaudited):				
Credit Suisse Securities (USA) LLC (2)	$	25,400	2	5.38%
UBS Securities LLC (2)	$	4,962	2	5.31%
Bear, Stearns International Limited	$	5,898	16	6.83%
Column Financial Inc, a subsidiary of Credit Suisse Securities (USA) LLC.	$	12,262	18	6.50%
December 31, 2005:				
Credit Suisse Securities (USA) LLC	$	31,158	17	4.34%
Bear, Stearns International Limited	$	36,044	17	5.51%
Deutsche Bank AG, Cayman Islands Branch	$	16,691	18	5.68%

(1) Equal to the estimated fair value of securities or loans sold, plus accrued interest income, minus the sum of repurchase agreement liabilities plus accrued interest expense.
(2) Facility was repaid in full as part of the sale of the Company's agency RMBS portfolio on October 2, 2006.

Repurchase and Credit Facilities

In August 2006, the Company's subsidiary, RCC Real Estate SPE 2, LLC, entered into a master repurchase agreement with Column Financial, Inc., a wholly-owned subsidiary of Credit Suisse Securities (USA) LLC, ("CS") to finance the purchase of commercial real estate loans. The maximum amount of the Company's borrowing under the repurchase agreement is $300.0 million. Each repurchase transaction specifies its own terms, such as identification of the assets subject to the transaction, sales price, repurchase price, rate and term. The Company has guaranteed RCC Real Estate SPE 2, LLC's obligations under the repurchase agreement to a maximum of $300.0 million. At September 30, 2006, the Company had borrowed $43.0 million, all of which was guaranteed, with a weighted average interest rate of LIBOR plus 1.17%, which was 6.50% at September 30, 2006.

In March 2006, the Company entered into a secured term credit facility with Bayerische Hypo - und Vereinsbank AG to finance the purchase of equipment leases and notes. The maximum amount of the Company's borrowing under this facility is $100.0 million.

Borrowings under this facility bear interest at one of two rates, determined by asset class:

- Pool A - one-month LIBOR plus 1.10%; or
- Pool B - one-month LIBOR plus 0.80%.

The facility expires March 2010. The Company paid $300,000 and $20,000 in commitment fees and unused fees as of September 30, 2006. Commitment fees are being amortized into interest expense using the effective yield method over the life of the facility and are recorded in the consolidated statements of operations. Unused fees are expensed immediately into interest expense and are recorded in the consolidated statements of operations. As of September 30, 2006, the Company had borrowed $87.1 million at a weighted average interest rate of 6.34%.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 7 - BORROWINGS – (Continued)

Repurchase and Credit Facilities (continued)

In December 2005, the Company's subsidiary, RCC Real Estate SPE, LLC, entered into a master repurchase agreement with Deutsche Bank AG, Cayman Islands Branch to finance the purchase of commercial real estate loans. The maximum amount of the Company's borrowing under the repurchase agreement is $300.0 million. Each repurchase transaction specifies its own terms, such as identification of the assets subject to the transaction, sales price, repurchase price, rate and term. The Company had guaranteed RCC Real Estate SPE's obligations under the repurchase agreement to a maximum of $30.0 million, which may be reduced based upon the amount of equity the Company has in the commercial real estate loans held on this facility. At September 30, 2006, no borrowings were outstanding under this facility. At December 31, 2005, the Company had borrowed $38.6 million with a weighted average interest rate of LIBOR plus 1.32%, which was 5.68% at December 31, 2005. The Company had no risk under this guaranty at September 30, 2006 and the Company's maximum risk under this guaranty was $30.0 million at December 31, 2005.

In December 2005, the Company entered into a $15.0 million unsecured revolving credit facility with Commerce Bank, N.A. This facility was increased to $25.0 million in April 2006. Outstanding borrowings bear interest at one of two rates elected at the Company's option; (i) the lender's prime rate plus a margin ranging from 0.50% to 1.50% based upon the Company's leverage ratio; or (ii) LIBOR plus a margin ranging from 1.50% to 2.50% based upon the Company's leverage ratio. The facility expires in December 2008. The Company paid $250,000 and $11,000 in commitment fees and unused line fees as of September 30, 2006. Commitment fees are being amortized into interest expense using the effective yield method over the life of the facility and are recorded in the consolidated statements of operations. Unused line fees are expensed immediately into interest expense and are recorded in the consolidated statements of operations. As of September 30, 2006, no borrowings were outstanding under this facility. At December 31, 2005, the balance outstanding was $15.0 million at an interest rate of 6.37%.

In August 2005, the Company's subsidiary, RCC Real Estate, Inc. ("RCC Real Estate"), entered into a master repurchase agreement with Bear, Stearns International Limited ("Bear Stearns") to finance the purchase of commercial real estate loans. The maximum amount of the Company's borrowing under the repurchase agreement is $150.0 million. Each repurchase transaction specifies its own terms, such as identification of the assets subject to the transaction, sales price, repurchase price, rate and term. The Company has guaranteed RCC Real Estate's obligations under the repurchase agreement to a maximum of $150.0 million. At September 30, 2006, the Company had borrowed $10.9 million, all of which was guaranteed, with a weighted average interest rate of LIBOR plus 1.50%, which was 6.83% at September 30, 2006. At December 31, 2005, the Company had borrowed $80.8 million with a weighted average interest rate of LIBOR plus 1.14%, which was 5.51% at December 31, 2005.

RCC Real Estate has received a waiver from Bear Stearns with respect to compliance with a financial covenant in the master repurchase agreement between it and Bear Stearns. The waiver was required due to the Company's net loss during the three months ended September 30, 2006, which was caused by the loss realized by the Company on the sale of the remainder of its portfolio of agency RMBS (see Note 4). Under the covenant, the Company is required to have no less than $1.00 of net income in any period of four consecutive calendar months. The waiver is effective through January 31, 2007.

At September 30, 2006, the Company has complied, to the best of its knowledge, with all of its other financial covenants under its debt agreements.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 7 - BORROWINGS – (Continued)

Repurchase and Credit Facilities (continued)

In March 2005, the Company entered into a master repurchase agreement with CS to finance the purchase of agency RMBS portfolio. Each repurchase transaction specifies its own terms, such as identification of the assets subject to the transaction, sales price, repurchase price, rate and term. At September 30, 2006, the Company had borrowed $577.2 million with a weighted average interest rate of 5.38%. On October 2, 2006, all outstanding borrowings under this facility were repaid in full in connection with the sale of the Company's agency RMBS portfolio. At December 31, 2005, the Company had borrowed $948.9 million with a weighted average interest rate of 4.34%.

In March 2005, the Company entered into a master repurchase agreement with UBS Securities LLC to finance the purchase of agency RMBS portfolio. Each repurchase transaction specifies its own terms, such as identification of the assets subject to the transaction, sales price, repurchase price, rate and term. At September 30, 2006, the Company had borrowed $139.1 million with a weighted average interest rate of 5.31%. On October 2, 2006, all outstanding borrowings under this facility were repaid in full in connection with the sale of the Company's remaining agency RMBS portfolio. At December 31, 2005, the Company had no borrowings under this agreement.

Collateralized Debt Obligations

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

The senior notes issued to investors by RREF 2006-1 consist of the following classes: (i) $129.4 million of class A-1 notes bearing interest at 1-month LIBOR plus 0.32%; (ii) $17.4 million of class A-2 notes bearing interest at 1-month LIBOR plus 0.35%; (iii) $5.0 million of class A-2 notes bearing interest at a fixed rate of 5.842%; (iv) $6.9 million of class B notes bearing interest at 1-month LIBOR plus 0.40%; (v) $20.7 million of class C notes bearing interest at 1-month LIBOR plus 0.62%; (vi) $15.5 million of class D notes bearing interest at 1-month LIBOR plus 0.80%; (vii) $20.7 million of class E notes bearing interest at 1-month LIBOR plus 1.30%; (viii) $19.8 million of class F notes bearing interest at 1-month LIBOR plus 1.60%; (ix) $17.3 million of class G notes bearing interest at 1-month LIBOR plus 1.90%; (x) $12.9 million of class H notes bearing interest at 1-month LIBOR plus 3.75%, (xi) $14.7 million of Class J notes bearing interest at a fixed rate of 6.00% and (xii) $28.4 million of Class K notes bearing interest at a fixed rate of 6.00%. As a result of the Company's ownership of the Class J and K senior notes, these notes eliminate in consolidation. All of the notes issued mature in August 2046, although the Company has the right to call the notes anytime after August 2016 until maturity. The weighted average interest rate on all notes issued to investors was 6.15% at September 30, 2006.

19

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 7 - BORROWINGS – (Continued)

Collateralized Debt Obligations – (Continued)

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

The senior notes issued to investors by Apidos CDO III consist of the following classes: (i) $212.0 million of class A-1 notes bearing interest at 3-month LIBOR plus 0.26%; (ii) $19.0 million of class A-2 notes bearing interest at 3-month LIBOR plus 0.45%; (iii) $15.0 million of class B notes bearing interest at 3-month LIBOR plus 0.75%; (iv) $10.5 million of class C notes bearing interest at 3-month LIBOR plus 1.75%; and (v) $6.0 million of class D notes bearing interest at 3-month LIBOR plus 4.25%. All of the notes issued mature on June 12, 2020, although the Company has the right to call the notes anytime after June 12, 2011 until maturity. The weighted average interest rate on all notes was 5.76% at September 30, 2006.

In August 2005, the Company closed Apidos CDO I, a $350.0 million CDO transaction that provides financing for bank loans. The investments held by Apidos CDO I collateralize the debt it issued and, as a result, the investments are not available to the Company, its creditors or stockholders. Apidos CDO I issued a total of $321.5 million of senior notes at par to investors and RCC Commercial purchased a $28.5 million equity interest representing 100% of the outstanding preference shares. The equity interest is subordinated in right of payment to all other securities issued by Apidos CDO I.

The senior notes issued to investors by Apidos CDO I consist of the following classes: (i) $265.0 million of class A-1 notes bearing interest at 3-month LIBOR plus 0.26%; (ii) $15.0 million of class A-2 notes bearing interest at 3-month LIBOR plus 0.42%; (iii) $20.5 million of class B notes bearing interest at 3-month LIBOR plus 0.75%; (iv) $13.0 million of class C notes bearing interest at 3-month LIBOR plus 1.85%; and (v) $8.0 million of class D notes bearing interest at a fixed rate of 9.251%. All of the notes issued mature on July 27, 2017, although the Company has the right to call the notes anytime after July 27, 2010 until maturity. The weighted average interest rate on all notes was 5.94% at September 30, 2006.

In July 2005, the Company closed Ischus CDO II, a $403.0 million CDO transaction that provides financing for mortgage-backed and other asset-backed securities. The investments held by Ischus CDO II collateralize the debt it issued and, as a result, those investments are not available to the Company, its creditors or stockholders. Ischus CDO II issued a total of $376.0 million of senior notes at par to investors and RCC Real Estate purchased a $27.0 million equity interest representing 100% of the outstanding preference shares. In August 2006, upon approval by the Company's Board of Directors, the preference shares of Ischus CDO II were transferred to the Company's wholly-owned subsidiary, RCC Commercial, Inc. ("RCC Commercial"). As of September 30, 2006, RCC Commercial owned a $27.0 million equity interest representing 100% of the outstanding preference shares. The equity interest is subordinate in right of payment to all other securities issued by Ischus CDO II.

The senior notes issued to investors by Ischus CDO II consist of the following classes: (i) $214.0 million of class A-1A notes bearing interest at 1-month LIBOR plus 0.27%; (ii) $50.0 million of class A-1B delayed draw notes bearing interest on the drawn amount at 1-month LIBOR plus 0.27%; (iii) $28.0 million of class A-2 notes bearing interest at 1-month LIBOR plus 0.45%; (iv) $55.0 million of class B notes bearing interest at 1-month LIBOR plus 0.58%; (v) $11.0 million of class C notes bearing interest at 1-month LIBOR plus 1.30%; and (vi) $18.0 million of class D notes bearing interest at 1-month LIBOR plus 2.85%. All of the notes issued mature on August 6, 2040, although the Company has the right to call the notes at par any time after August 6, 2009 until maturity. The weighted average interest rate on all notes was 5.62% at September 30, 2006.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 7 - BORROWINGS – (Continued)

Trust Preferred Securities

In May 2006 and September 2006, the Company formed Resource Capital Trust I (“RCTI”) and RCC Trust II (“RCTII”), respectively, for the sole purpose of issuing and selling trust preferred securities. In accordance with FASB Interpretation No. 46R (“FIN 46R”), RCTI and RCTII are not consolidated into the Company’s consolidated financial statements because the Company is not deemed to be the primary beneficiaries of these entities. The Company owns 100% of the common shares in RCTI and RCTII. Each respective trust issued $25.0 million of preferred shares to unaffiliated investors.

In connection with the issuance and sale of the trust preferred securities, the Company issued junior subordinated debentures to RCTI and RCTII of $25.8 million each, representing the Company’s maximum exposure to loss. The debt issuance costs associated with the junior subordinated debentures for RCTI and RCTII at September 30, 2006 were $829,000 and $828,000, respectively. These costs are being amortized into interest expense using the effective yield method over a ten year period and are recorded in the consolidated statements of operations.

The rights of holders of common shares of RCTI and RCTII are subordinate to the rights of the holders of preferred shares only in the event of a default; otherwise, the common shareholders’ economic and voting rights are pari passu with the preferred shareholders. The preferred and common securities of RCTI and RCTII are subject to mandatory redemption upon the maturity or call of the junior subordinated debentures. Unless earlier dissolved, RCTI will dissolve on May 25, 2041 and RCTII will dissolve on September 29, 2041. The junior subordinated debentures are the sole asset of RCTI and RCTII and mature on June 30, 2036 and October 30, 2036, respectively, and may be called at par by the Company any time after June 30, 2011 and October 30, 2011, respectively. Interest is payable for RCTI and RCTII quarterly at a floating rate equal to three-month LIBOR plus 3.95% per annum. The rates for RCTI and RCTII, at September 30, 2006, were 9.45% and 9.32%, respectively. The Company records its investments in RCTI and RCTII’s common shares of $774,000 each as investments in unconsolidated trusts and records dividend income upon declaration by RCTI and RCTII.

NOTE 8 - CAPITAL STOCK AND EARNINGS PER SHARE

The Company had authorized 500,000,000 shares of common stock, par value $0.001 per share, of which 17,821,434 and 15,682,334 shares (including 234,224 and 349,000 restricted shares) were outstanding as of September 30, 2006 and December 31, 2005, respectively.

On March 8, 2005, the Company granted 345,000 shares of restricted common stock and options to purchase 651,666 common shares at an exercise price of $15.00 per share, to the Manager. One third of the shares of restricted stock and options vested on March 8, 2006. The Company also granted 4,000 shares of restricted common stock to the Company’s four non-employee directors as part of their annual compensation. These shares vested in full on March 8, 2006. On March 8, 2006, the Company granted 4,224 shares of restricted stock to the Company’s four non-employee directors as part of their annual compensation. These shares vest in full on March 8, 2007.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 8 - CAPITAL STOCK AND EARNINGS PER SHARE – (Continued)

The following table summarizes restricted common stock transactions:

	Manager	Non-Employee Directors	Total
Unvested shares as of December 31, 2005	345,000	4,000	349,000
Issued	–	4,224	4,224
Vested	(115,000)	(4,000)	(119,000)
Forfeited	–	–	–
Unvested shares as of September 30, 2006 (Unaudited)	230,000	4,224	234,224

Pursuant to SFAS No. 123(R), the Company is required to value any unvested shares of restricted common stock granted to the Manager at the current market price. The estimated fair value of the shares of restricted stock granted, including shares issued to the four non-employee directors, was $5.3 million and $5.2 million at September 30, 2006 and December 31, 2005, respectively.

The following table summarizes common stock option transactions:

	Number of Options	Weighted Average Exercise Price
Outstanding as of December 31, 2005	651,666	$ 15.00
Granted	–	$ –
Exercised	–	$ –
Forfeited	–	$ –
Outstanding as of September 30, 2006 (Unaudited)	651,666	$ 15.00

None of the common stock options outstanding were exercised at September 30, 2006 and December 31, 2005, respectively. As of September 30, 2006, 722 common stock options were exercisable, and no common stock options were exercisable as of December 31, 2005. The common stock options are valued using the Black-Scholes model using the following assumptions:

	September 30, 2006 (Unaudited)	December 31, 2005
Expected life	9 years	10 years
Discount rate	4.694%	4.603%
Volatility	21.27%	20.11%
Dividend yield	10.40%	12.00%

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 8 - CAPITAL STOCK AND EARNINGS PER SHARE – (Continued)

The estimated fair value of the total common stock options was $386,200 and $158,300 at September 30, 2006 and December 31, 2005, respectively. The estimated fair value of each option grant at September 30, 2006 and December 31, 2005, respectively, was $0.655 and $0.243. For the three months ended September 30, 2006 and 2005, nine months ended September 30, 2006 and the period from March 8, 2005 (date operations commenced) through September 30, 2005 (hereafter referred to as period ended September 30, 2005), the components of equity compensation expense are as follows (in thousands):

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Period Ended September 30, 2005
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
Options granted to Manager	$ 86	$ 24	$ 208	$ 55
Restricted shares granted to Manager	697	797	1,367	1,784
Restricted shares granted to non-employee directors	15	15	45	34
Total equity compensation expense	$ 798	$ 836	$ 1,620	$ 1,873

During the three and nine months ended September 30, 2006, the Manager received 6,252 and 14,076 shares, respectively, as incentive compensation, valued at $79,000 and $194,000, respectively, pursuant to the management agreement. No incentive fee compensation shares were issued as of December 31, 2005.

In connection with the July 2006 hiring of a commercial mortgage direct loan origination team by Resource Real Estate, Inc. (see Related Party Transactions - Note 9), the Company agreed to issue up to 100,000 shares of common stock and options to purchase an additional 100,000 shares of common stock, if certain loan origination performance thresholds are achieved. The performance thresholds are two-tiered. Upon the achievement of $400.0 million of direct loan originations of commercial real estate loans, 60,000 restricted shares of common stock and options to purchase an additional 60,000 shares of common stock are issuable. Upon the achievement of another $300.0 million of direct loan originations of commercial real estate loans, a second tranche of 40,000 restricted shares of common stock and options to purchase another 40,000 shares of common stock are issuable. The restricted shares and options to purchase shares of common stock vest over a two-year period after issuance. The Company accounts for equity instruments issued to non-employees for goods or services in accordance with the provisions of SFAS No. 123(R) and Emerging Task Force Issue No. 96-18, *Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services* ("EITF 96-18"). Accordingly, when the non-employees complete their performance or when a performance commitment is reached, the Company is required to measure the fair value of the equity instruments. No expense was recognized for the three months ended September 30, 2006, as neither a performance commitment nor completion of performance was achieved.

Index

RESOURCE CAPITAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 – (Continued)
(Unaudited)

NOTE 8 - CAPITAL STOCK AND EARNINGS PER SHARE – (Continued)

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

	Three Months Ended September 30,	Nine Months Ended September 30,