

GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates in the financial statements include the valuation of our investments in revenue bonds and interest rate swap agreements.

The consolidated financial statements include the accounts of CharterMac and its majority owned subsidiary business trusts and corporations which it controls. We also own approximately 87% of PWF and 100% of Related through our wholly owned subsidiary, CM Corp. All inter-company accounts and transactions have been eliminated in consolidation. Unless otherwise indicated, the “Company”, as hereinafter used, refers to CharterMac and its consolidated subsidiaries.

Reclassifications

Certain amounts from prior years have been reclassified to conform to the 2003 presentation.

Significant Accounting Policies

Investment in revenue bonds

We account for our investments in revenue bonds as available-for-sale debt securities under the provisions of Statement of Financial Accounting Standards No. 115, “Accounting for Certain Investments in Debt and Equity Securities” (“SFAS 115”) due to a provision in most of our revenue bonds under which we have a right to require redemption of the revenue bonds prior to their maturity, although we can and may elect to hold them up to their maturity dates unless otherwise modified. As such, SFAS 115 requires us to classify these investments as “available-for-sale.” Accordingly, investments in revenue bonds are carried at their estimated fair values, with unrealized gains and losses reported in accumulated other comprehensive income. Unrealized gains or losses do not affect the cash flow generated from property operations, distributions to shareholders, the characterization of the tax-exempt income stream or the financial obligations under the revenue bonds.

If in our judgment, we determine it is probable that we will not receive all contractual payments required, when they are due, the revenue bond is deemed impaired and is written down to its then estimated fair value, with the amount of the write-down accounted for as a realized loss.

Because revenue bonds have a limited market, we estimate fair value for each bond as the present value of its expected cash flows using a discount rate for comparable tax-exempt investments. This process is based upon projections of future economic events affecting the real estate collateralizing the bonds, such as property occupancy rates, rental rates, operating cost inflation, market capitalization rates and an appropriate market rate of

interest, all of which are based on good faith estimates and assumptions we develop. Changes in market conditions and circumstances may occur which would cause these estimates and assumptions to change; therefore, actual results may vary from the estimates and the variance may be material.

For certain revenue bonds, management believes that certain factors have impacted the near-term fair value. In these instances, the revenue bonds are valued at either the outstanding face amount of the bond or management's estimate of the fair value, whichever is lower.

Equity Investments

Equity investments in other assets on the consolidated balance sheets include the following:

Investment in ARCap - Our preferred equity investment in ARCap Investors, L.L.C. (“ARCap”) is accounted for using the equity method because we have the ability to exercise significant influence, but not control, over ARCap’s operating and financial policies.

Cash and Cash Equivalents

Cash and cash equivalents includes cash in banks and investments in short-term instruments with an original maturity of three months or less. Certain amounts of cash and cash equivalents are restricted and serve as additional collateral for borrowings within our existing securitization programs.

Mortgage Banking Activities

PWF is an approved seller/servicer of multi-family mortgage loans for Fannie Mae, Freddie Mac, FHA and the Government National Mortgage Association (“Ginnie Mae”). For Fannie Mae, PWF is approved under the Delegated Underwriting and Servicing (“DUS”) program. Under DUS, upon obtaining a commitment from Fannie Mae with regard to a particular loan, Fannie Mae commits to acquire the mortgage loan based upon PWF's underwriting and PWF agrees to bear a portion of the risk of potential losses in the event of a default. Fannie Mae commitments may be made to acquire the mortgage loan for cash or in exchange for a mortgage-backed security backed by the mortgage loan. As a Program Plus lender for Freddie Mac, Freddie Mac agrees to acquire for cash from PWF loans for which PWF has issued commitments. Ginnie Mae agrees to exchange FHA-insured mortgages originated by PWF for Ginnie Mae securities.

Mortgage loans originated for Fannie Mae, Freddie Mac or Ginnie Mae are closed in the name of PWF, which uses corporate cash obtained by borrowing from a warehouse lender to fund the loans. Approximately a week to a month following closing of a loan, loan documentation and an assignment are delivered to Fannie Mae, Freddie Mac, Ginnie Mae, or a document custodian on its behalf and the cash purchase price or mortgage-backed security is delivered to PWF. PWF uses the cash it receives to