SUN COMMUNITIES INC
Form 10-Q
August 08, 2008
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

[X]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

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

Commission file number 1-12616

SUN COMMUNITIES, INC.

(Exact Name of Registrant as Specified in its Charter)

Maryland	**38-2730780**
(State of Incorporation)	(I.R.S. Employer Identification No.)
27777 Franklin Rd.	
Suite 200	
Southfield, Michigan	**48034**
(Address of Principal Executive Offices)	(Zip Code)

(248) 208-2500
(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. Yes[X] 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. (Check one):

Large accelerated filer [ ]   Accelerated filer [X]   Non-accelerated filer [ ]   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 [X]

Number of shares of Common Stock, $0.01 par value per share, outstanding

as of June 30, 2008: 18,403,927

SUN COMMUNITIES, INC.

INDEX

SUN COMMUNITIES, INC.

CONSOLIDATED BALANCE SHEETS

AS OF JUNE 30, 2008 AND DECEMBER 31, 2007

(amounts in thousands, except per share data)

	(Unaudited) June 30, 2008	December 31, 2007
ASSETS		
Investment property, net	$1,116,709	$1,134,204
Cash and cash equivalents	4,313	5,415
Inventory of manufactured homes	9,252	12,082
Investment in affiliate	7,450	20,000
Notes and other receivables	46,173	36,846
Other assets	37,116	37,276
TOTAL ASSETS	$1,221,013	$1,245,823
LIABILITIES		
Debt	$1,118,907	$1,101,972
Lines of credit	75,498	85,703
Other liabilities	37,336	32,102
TOTAL LIABILITES	1,231,741	1,219,777
Commitments and contingencies	—	—
Minority interest	724	4,999
STOCKHOLDERS' EQUITY (DEFICIT)		
Preferred stock, $0.01 par value, 10,000 shares authorized, none issued	$—	$—
Common stock, $0.01 par value, 90,000 shares authorized (June 30, 2008 and December 31, 2007, 20,206 and 20,228 shares issued respectively)	202	202
Additional paid-in capital	459,430	458,487
Officer's notes	(8,543)	(8,740)
Accumulated other comprehensive loss	(924)	(856)
Distributions in excess of accumulated earnings	(398,017)	(364,446)
Treasury stock, at cost (June 30, 2008 and December 31, 2007, 1,802 shares)	(63,600)	(63,600)
TOTAL STOCKHOLDERS' EQUITY (DEFICIT)	(11,452)	21,047
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)	$1,221,013	$1,245,823

The accompanying notes are an integral part of the consolidated financial statements

- 3 -

SUN COMMUNITIES, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE PERIODS ENDED JUNE 30, 2008 AND 2007

(amounts in thousands, except for per share data)

(unaudited)

	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
REVENUES				
Income from real property	$47,846	$46,634	$98,399	$96,100
Revenue from home sales	8,768	6,205	16,271	12,355
Rental home revenue	5,136	4,696	10,132	9,135
Ancillary revenues, net	88	88	314	351
Interest	807	667	1,612	1,456
Other income (loss)	2,829	(344)	3,700	(94)
Total revenues	65,474	57,946	130,428	119,303
COSTS AND EXPENSES				
Property operating and maintenance	12,615	11,907	24,976	23,853
Real estate taxes	4,170	4,097	8,339	8,195
Cost of home sales	6,981	4,832	12,820	9,756
Rental home operating and maintenance	3,965	3,299	7,431	6,439
General and administrative - real property	4,713	3,762	8,885	8,147
General and administrative - home sales and rentals	1,715	1,320	3,327	2,978
Depreciation and amortization	16,355	15,582	32,360	30,932
Interest	14,570	15,212	29,950	30,381
Interest on mandatorily redeemable debt	844	892	1,688	1,809
Total expenses	65,928	60,903	129,776	122,490
Income (loss) from affiliate	(7,720)	541	(12,550)	848
Loss before income tax and minority interest	(8,174)	(2,416)	(11,898)	(2,339)
Less: Provision (benefit) for state income taxes	128	25	(107)	50
Loss from operations	(8,302)	(2,441)	(11,791)	(2,389)
Less: Loss allocated to minority interest	(934)	(278)	(1,328)	(272)
Net loss	$(7,368)	$(2,163)	$(10,463)	$(2,117)
Weighted average common shares outstanding:				
Basic	18,162	17,923	18,119	17,882
Diluted	18,162	17,923	18,119	17,882
Basic and diluted net loss per share:	$(0.41)	$(0.12)	$(0.58)	$(0.12)
Cash dividends per common share:	$0.63	$0.63	$1.26	$1.26

The accompanying notes are an integral part of the consolidated financial statements

SUN COMMUNITIES, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

FOR THE PERIODS ENDED JUNE 30, 2008 AND 2007

(amounts in thousands)

(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Net loss	$(7,368)	$(2,163)	$(10,463)	$(2,117)
Unrealized gain (loss) on interest rate swaps	1,348	656	(68)	402
Comprehensive loss	$(6,020)	$(1,507)	$(10,531)	$(1,715)

SUN COMMUNITIES, INC.

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

FOR THE SIX MONTHS ENDED JUNE 30, 2008

(amounts in thousands, except per share data)

(unaudited)

	Common Stock	Additional Paid-in Capital	Officer's Notes	Accumulated Other Comprehensive Loss	Distributions in Excess of Accumulated Earnings	Treasury Stock	Total Equity (Deficit)
Balance as of December 31, 2007	$ 202	$ 458,487	$ (8,740)	$ (856)	$ (364,446)	$ (63,600)	$ 21,047
Cancellation of common stock, net	—	(359)	—	—	(1)	—	(360)
Stock-based compensation - amortization and forfeitures	—	1,302	—	—	45	—	1,347
Repayment of officer's notes	—	—	197	—	—	—	197
Net loss	—	—	—	—	(10,463)	—	(10,463)
Unrealized loss on interest rate swaps	—	—	—	(68)	—	—	(68)

Cash distributions declared of $1.26 per share	—	—	—	—	(23,152)	—	(23,152)
Balance as of June 30, 2008	$ 202	$ 459,430	$ (8,543)	$ (924)	$ (398,017)	$ (63,600)	$ (11,452)

The accompanying notes are an integral part of the consolidated financial statements

SUN COMMUNITIES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX MONTHS ENDED JUNE 30, 2008 AND 2007

(amounts in thousands)

(unaudited)

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (10,463)	$ (2,117)
Adjustments to reconcile net loss to cash provided by operating activities:		
Loss allocated to minority interests	(1,328)	(272)
Gain from land disposition	(3,303)	—
Gain on valuation of derivative instruments	(2)	(250)
Stock compensation expense	1,354	1,354
Depreciation and amortization	34,383	32,490
Amortization of deferred financing costs	749	720
Distributions from affiliate	—	500
Equity (income) loss from affiliate	12,550	(848)
Increase in notes receivable from sale of homes	(1,183)	(465)
Increase in inventory, other assets and other receivables, net	(9,231)	(7,032)
Increase in accounts payable and other liabilities	2,585	2,116
Net cash provided by operating activities	26,111	26,196
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investment in rental properties	(14,521)	(10,068)
Proceeds related to disposition of land and other assets	6,461	—
Decrease in notes receivable and officer's notes, net	884	12,897
Net cash provided by (used in) investing activities	(7,176)	2,829
CASH FLOWS FROM FINANCING ACTIVITIES:		
Redemption of common stock and OP units	(360)	(1,259)
Proceeds from option exercise	—	38
Borrowings on lines of credit	49,544	43,402
Repayments on lines of credit	(59,749)	(73,666)
Payments to retire preferred operating partnership units	—	(4,500)
Payments to redeem notes payable and other debt	(10,112)	(8,177)
Proceeds from notes payable and other debt	27,000	37,500
Payments for deferred financing costs	(308)	(341)
Distributions	(26,052)	(22,391)
Net cash used in financing activities	(20,037)	(29,394)
Net decrease in cash and cash equivalents	(1,102)	(369)
Cash and cash equivalents, beginning of period	5,415	3,183
Cash and cash equivalents, end of period	$ 4,313	$ 2,814
SUPPLEMENTAL INFORMATION:		
Cash paid for interest	$ 28,248	$ 29,881
Cash paid for interest on mandatorily redeemable debt	$ 1,740	$ 1,781

Noncash investing and financing activities:		
Unrealized gain (loss) on interest rate swaps	$ (68)	$ 402
Rental homes transferred from inventory	$ 7,914	$ 6,877
Rental home sales financed by Company	$ 6,968	$ 4,688

The accompanying notes are an integral part of the consolidated financial statements

1. Basis of Presentation

These unaudited consolidated financial statements of Sun Communities, Inc., a Maryland corporation, (the “Company”) and all majority-owned and controlled subsidiaries including Sun Communities Operating Limited Partnership (the “Operating Partnership”), SunChamp LLC (“SunChamp”), and Sun Home Services, Inc. (“SHS”), have been prepared pursuant to the Securities and Exchange Commission (“SEC”) rules and regulations and should be read in conjunction with the consolidated financial statements and accompanying notes of the Company included in Annual Report on Form 10-K for the year ended December 31, 2007. The following notes to consolidated financial statements present interim disclosures as required by the SEC. The accompanying consolidated financial statements reflect, in the opinion of management, all adjustments necessary for a fair presentation of the interim financial statements. All such adjustments are of a normal and recurring nature. Certain reclassifications have been made to prior periods’ financial statements in order to conform to current period presentation.

2. Investment Property

The following table sets forth certain information regarding investment property (amounts in thousands):

	(Unaudited) June 30, 2008	**December 31, 2007**
Land	$ 117,116	$ 117,310
Land improvements and buildings	1,188,674	1,184,257
Rental homes and improvements	177,576	170,227
Furniture, fixtures, and equipment	36,577	36,433
Land held for future development	28,036	30,199
	1,547,979	1,538,426
Less accumulated depreciation	(431,270)	(404,222)
Investment property, net	$ 1,116,709	$ 1,134,204

Land improvements and buildings consist primarily of infrastructure, roads, landscaping, clubhouses, maintenance buildings and amenities.

The Company sold approximately 70 acres of undeveloped land that resulted in a $2.6 million gain through the three months ended June 30, 2008. The Company sold approximately 82 acres of undeveloped land that resulted in a $3.3 million gain through the six months ended June 30, 2008.

3. Notes and Other Receivables

The following table sets forth certain information regarding notes and other receivables (amounts in thousands):

	June 30, 2008	December 31, 2007
Installment loans on manufactured homes with interest payable monthly at a net weighted average interest rate and maturity of 7.8% and 13.3 years and 7.3% and 13.2 years at June 30, 2008, and December 31, 2007, respectively.	$ 37,893	$ 30,429
Other receivables, net of allowance for losses of $0.3 million at June 30, 2008 and December 31, 2007.	8,280	6,417
Total notes and other receivables, net	$ 46,173	$ 36,846

SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

3. Notes and Other Receivables, continued

The installment loans of $37.9 million and $30.4 million at June 30, 2008 and December 31, 2007, respectively, are collateralized by manufactured homes and are presented net of allowance for losses of $0.2 million at June 30, 2008 and December 31, 2007. The loans represent financing provided by the Company to purchasers of manufactured homes located in its communities.

Officer’s notes, presented as a reduction to stockholders’ equity in the balance sheet, are 10 year, LIBOR + 1.75% notes, with a minimum and maximum interest rate of 6% and 9%, respectively. The notes become due in three installments on each of December 31, 2008, 2009 and 2010. The following table sets forth certain information regarding officer’s notes as of June 30, 2008, and December 31, 2007 (in thousands except for shares and units):

	As of June 30, 2008			As of December 31, 2007		
		Secured by			Secured by	
Promissory Notes	Outstanding Principal Balance	Common Stock	Common OP Units	Outstanding Principal Balance	Common Stock	Common OP Units
Secured - $1.3 million	$ 987	60,750	—	$ 1,010	62,151	—
Secured - $6.6 million	5,015	134,893	97,044	5,132	138,003	99,282
Secured - $1.0 million	777	71,814	—	794	73,470	—
Unsecured - $1.0 million	777	—	—	794	—	—
Unsecured - $1.3 million	987	—	—	1,010	—	—
Total promissory notes	$ 8,543	267,457	97,044	$ 8,740	273,624	99,282

The officer’s personal liability on the secured promissory notes is limited to all accrued interest on such notes plus fifty percent (50%) of the deficiency, if any, after application of the proceeds from the sale of the secured shares and/or the secured units to the then outstanding principal balance of the promissory notes. The unsecured notes are fully recourse to the officer.

The reduction in the aggregate principal balance of these notes was $0.2 million for the six months ended June 30, 2008 and 2007. Total interest was $0.1 million and $0.2 million for the three months ended June 30, 2008 and 2007, respectively. Total interest was $0.3 million for the six months ended June 30, 2008 and 2007.

4. Investment in Affiliate

Prior to March 2008, Origen Financial, Inc. (“Origen”) was a real estate investment trust that was in the business of originating and servicing manufactured home loans. In October 2003, the Company purchased 5,000,000 shares of common stock of Origen for $50 million. The Company owns approximately 19% of Origen at June 30, 2008, and its investment is accounted for using the equity method of accounting.

The Company determined that its investment in Origen had been adversely impacted by market conditions, and reduced the carrying value of its investment to reflect a fair value of $7.5 million based on the closing price of $1.49 per share as of June 30, 2008. Equity loss from affiliate recorded for the three months ended June 30, 2008, reflects the Company’s estimate of its portion of the anticipated loss from Origen of $0.9 million, as well as an other than temporary impairment loss of $6.8 million. Equity loss from affiliate recorded for the six months ended June 30, 2008, reflects the Company’s estimate of its portion of the anticipated loss from Origen of $5.8 million, as well as an other than temporary impairment loss of $6.8 million.

SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

4. Investment in Affiliate, continued

On March 13, 2008, Origen announced that recent and current conditions in the credit markets have adversely impacted Origen's business and financial condition to the extent that it has determined to suspend loan originations for its own account and has taken steps to right-size its work force. Subsequently, Origen announced that it sold its unsecuritized loans with an aggregate carrying amount of approximately $176 million for net proceeds of approximately $155 million and completed a $46 million secured financing arrangement provided by an affiliate of one of Origen's principal stockholders. Origen used the proceeds from these transactions to pay off its warehouse facility and supplemental advance facility.

On April 30, 2008, Origen announced that it entered into an agreement for the sale of its servicing platform assets. The sale was approved by Origen's stockholders at its annual meeting on June 25, 2008, as one component of an Asset Disposition and Management Plan. Other components of this plan include the active management of Origen's securitized loan portfolios and other remaining assets and the continued rationalizing of operating costs as necessary and appropriate to efficiently and effectively continue operations and preserve stockholder value.

Origen announced July 2, 2008 that it had completed the previously announced sale of its servicing platform assets to Green Tree Servicing LLC, a leading servicer of manufactured housing loans, other residential and consumer loans.

5. Debt

The following table sets forth certain information regarding debt (amounts in thousands):

	June 30, 2008	December 31, 2007
Collateralized term loans - CMBS, 4.93-5.32%, due July 1, 2011-2016	$ 482,531	$ 486,063
Collateralized term loans - FNMA, of which $102.4M is variable, due April 28, 2014 and January 1, 2015, at the Company's option, interest at 3.59 - 5.20% at June 30, 2008 and 4.51 - 5.20% at December 31, 2007.	379,643	381,587
Preferred OP units, redeemable at various dates from December 1, 2009 through January 2, 2014, average interest at 6.8% at June 30, 2008, and 7.2% at December 31, 2007.	49,447	49,447
Mortgage notes, other, maturing at various dates from June 1, 2009 through May 1, 2017, average interest at 5.66% at June 30, 2008 and 6.10% at	207,286	184,875

December 31, 2007.

Total debt	$ 1,118,907	$ 1,101,972

The collateralized term loans totaling $862.2 million at June 30, 2008, are secured by 87 properties comprising approximately 31,124 sites representing approximately $569.0 million of net book value. The mortgage notes totaling $207.3 million at June 30, 2008, are collateralized by 18 communities comprising approximately 6,420 sites representing approximately $184.0 million of net book value.

The Company has an unsecured revolving line of credit facility with a maximum borrowing capacity of $115 million, subject to certain borrowing base calculations. The outstanding balance on the line of credit at June 30, 2008 and December 31, 2007, was $70.8 million and $85.4 million, respectively. In addition, $3.4 million of availability was used to back standby letters of credit at June 30, 2008 and December 31, 2007. Borrowings under the line of credit bear an interest rate of LIBOR plus 1.65% (4.13% at June 30, 2008) and mature October 1, 2010. A one year extension is available at the Company’s option. At June 30, 2008 and December 31, 2007, $40.8 million and $26.2 million, respectively, were available to be drawn under the facility based on the calculation of the borrowing base at each period.

SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

5. Debt, continued

The Company also has a $40.0 million floor plan facility that allows for draws on new and pre-owned home purchases and on the Company's portfolio of rental homes. At June 30, 2008 and December 31, 2007, the outstanding balance on the floor plan was $4.7 million and $0.3 million, respectively. The facility matures on March 1, 2009, and bears interest at Prime for borrowings on new homes (5.00% at June 30, 2008) and Prime plus 0.50% for borrowings on pre-owned and rental homes. Prime means for any month, the prevailing "prime rate" as quoted in the Wall Street Journal on last day of such calendar month.

During the quarter, the Company completed a financing of $27.0 million with a bank. The loan has a three year term, with a two year extension at the Company's option. The terms of the loan require interest only payments for the first year, with the remainder of the term being amortized based on a 30 year table. The interest rate is 205 basis points over LIBOR, or 4.85 percent. The proceeds from the financing were used to repay an existing mortgage note of $4.3 million with the remainder used to pay down the Company's lines of credit.

At June 30, 2008, the total of maturities and amortization of debt and lines of credit during the next five years, are as follows (in thousands):

		Maturities and Amortization By Period					
	Total Due	Jul 2008- Jun 2009	Jul 2009 - Jun 2010	Jul 2010 - Jun 2011	Jul 2011 - Jun 2012	Jul 2012 - Jun 2013	After 5 years
Debt	$1,118,907	$23,291	$21,900	$44,777	$129,943	$12,554	$886,442
Lines of credit	75,498	4,698	—	70,800	—	—	—
Total	$1,194,405	$27,989	$21,900	$115,577	$129,943	$12,554	$886,442

The most restrictive of the Company's debt agreements place limitations on secured and unsecured borrowings and contain minimum debt service coverage, leverage, distribution and net worth requirements. At June 30, 2008, and December 31, 2007, the Company was in compliance with all covenants.

6. Share-Based Compensation

The Company's primary share-base compensation is restricted stock. In February 2008, the Company issued twenty five thousand shares of restricted stock to certain key employees. The awards vest over a 10 year period beginning on the fourth anniversary of the grant date and have a weighted average grant date fair value of $19.92 per share.

The Company had previously granted phantom liability and equity awards that were contingent upon achieving certain performance targets. These performance-based stock awards were cancelled during the first quarter of 2008.

On July 10, 2008 the Company entered into a Retirement from Employment and Release Agreement (“Retirement Agreement”) with Brian W. Fannon, the Company’s President. Pursuant to the Retirement Agreement, all of Mr. Fannon’s outstanding stock options and other stock based compensation awards became fully vested and immediately exercisable. This change in terms is considered a modification per SFAS No. 123R (revised 2004) “Share-Based Payment”. As the terms and conditions were accepted by Mr. Fannon prior to June 30, 2008 the compensation expense has been recorded in the current period.

SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

7. Other Income

The components of other income are summarized as follows (in thousands):

	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
Brokerage commissions	$ 168	$ 170	$ 360	$ 373
Gain on sale of undeveloped land	2,604	—	3,303	—
Gain (loss) on disposition of assets, net	74	(471)	87	(469)
Other	(17)	(43)	(50)	2
Total other income (loss)	$ 2,829	$ (344)	$ 3,700	$ (94)

8. Segment Reporting

The consolidated operations of the Company can be segmented into home sales and home rentals and real property operations segments. A presentation of segment financial information is summarized as follows (amounts in thousands):

	Three months ended June 30, 2008			Six months ended June 30, 2008		
	Real Property Operations	Home Sales and Home Rentals	Consolidated	Real Property Operations	Home Sales and Home Rentals	Consolidated
Revenues	$ 47,846 (2)	$ 13,904	$ 61,750	$ 98,399 (2)	$ 26,403	$ 124,802
Operating expenses/Cost of sales	16,785	10,946	27,731	33,315	20,251	53,566
Net operating income [1]/Gross profit	31,061	2,958	34,019	65,084	6,152	71,236
Adjustments to arrive at net loss:						
Other revenues	3,640	84	3,724	4,607	1,019	5,626
General and administrative	(4,713)	(1,715)	(6,428)	(8,885)	(3,327)	(12,212)
Depreciation and amortization	(11,697)	(4,658)	(16,355)	(23,147)	(9,213)	(32,360)
Interest expense	(15,330)	(84)	(15,414)	(31,515)	(123)	(31,638)
Equity loss from affiliate	(7,720)	—	(7,720)	(12,550)	—	(12,550)
Benefit (provision) for state income taxes	(128)	—	(128)	107		