AMERICAN LAND LEASE INC
Form 10-Q
August 07, 2008

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 June 30, 2008

OR

¨ ***TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934***
Commission file number 1-9360

AMERICAN LAND LEASE, INC.

(Exact name of registrant as specified in its charter)

Delaware	***84-1038736***
(State or other jurisdiction of	***(IRS Employer***
Incorporation or organization)	***Identification No.)***
29399 U.S. Hwy 19 North, Suite 320	
Clearwater, Florida	***33761***
(Address of Principal Executive Offices)	***(Zip Code)***

Registrant s telephone number, including area code (727) 726-8868

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. 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 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

As of August 4, 2008, approximately 7,938,000 shares of common stock, par value $.01 per share, were outstanding.

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AMERICAN LAND LEASE, INC. AND SUBSIDIARIES

FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2008

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PART I.

FINANCIAL INFORMATION

Item 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

AMERICAN LAND LEASE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except per share data)

	June 30, 2008 (unaudited)	December 31, 2007
ASSETS		
Real estate, net of accumulated depreciation of $34,145 and $31,842, respectively, including real estate under development of $128,277 and $122,403, respectively	$ 406,520	$ 399,517
Cash and cash equivalents	142	541
Inventory	15,841	20,084
Other assets, net	17,999	16,391
Total Assets	$ 440,502	$ 436,533
LIABILITIES		
Secured notes payable	$ 259,630	$ 239,970
Secured credit facilities	21,219	30,932
Accounts payable and accrued liabilities	8,196	9,288
	289,045	280,190
MINORITY INTEREST IN OPERATING PARTNERSHIP	16,824	17,339
STOCKHOLDERS EQUITY		
Preferred stock, par value $.01 per share; 3,000 shares authorized; 1,000 and 1,000 shares issued and outstanding, respectively	25,000	25,000
Common stock, par value $.01 per share; 12,000 shares authorized; 9,595 and 9,485 shares issued, respectively; 7,625 and 7,553 shares outstanding (excluding treasury stock), respectively	96	95
Additional paid-in capital	295,266	293,821
Dividends in excess of accumulated earnings	(153,810)	(148,749)
Treasury stock, 1,970 and 1,932 shares at cost, respectively	(31,919)	(31,163)
	134,633	139,004
Total Liabilities and Stockholders Equity	$ 440,502	$ 436,533

See Notes to Condensed Consolidated Financial Statements

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AMERICAN LAND LEASE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except 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
RENTAL PROPERTY OPERATIONS				
Rental and other property revenues	$ 9,733	$ 9,334	$ 19,450	$ 18,670
Golf course operating revenues	217	219	656	649
Total property operating revenues	9,950	9,553	20,106	19,319
Property operating expenses	(3,156)	(3,111)	(6,319)	(6,300)
Golf course operating expenses	(348)	(357)	(680)	(692)
Total property operating expenses	(3,504)	(3,468)	(6,999)	(6,992)
Depreciation	(1,351)	(1,227)	(2,699)	(2,432)
Income from rental property operations	5,095	4,858	10,408	9,895
SALES OPERATIONS				
Home sales revenue	3,525	7,929	7,380	15,594
Cost of home sales	(2,814)	(5,658)	(5,651)	(11,291)
Gross profit on home sales	711	2,271	1,729	4,303
Commissions earned on brokered sales	39	44	84	119
Commissions paid on brokered sales	(23)	(19)	(42)	(54)
Gross profit on brokered sales	16	25	42	65
Selling and marketing expenses	(1,519)	(2,375)	(3,557)	(4,712)
Loss from sales operations	(792)	(79)	(1,786)	(344)
General and administrative expenses	(1,233)	(993)	(2,455)	(1,957)
Interest and other income	58	8	102	178
Loss on early debt retirement			(1,987)	
Interest expense	(2,198)	(2,142)	(4,446)	(4,251)
Income (loss) before minority interest in Operating Partnership and discontinued operations	930	1,652	(164)	3,521
Minority interest in Operating Partnership	(108)	(188)	19	(399)
Income (loss) from continuing operations	822	1,464	(145)	3,122
DISCONTINUED OPERATIONS				
Discontinued operations		109		220
Depreciation on discontinued operations		(24)		(48)
Minority interest in Operating Partnership attributable to discontinued operations		(10)		(20)
Income from discontinued operations, net of minority interest in Operating Partnership		75		152

Net income (loss)		822		1,539		(145)		3,274
Cumulative preferred stock dividends		(485)		(485)		(969)		(969)
Net income (loss) available to common stockholders	$	337	$	1,054	$	(1,114)	$	2,305
Earnings per common share basic:								
Income (loss) from continuing operations (net of preferred stock dividends)	$	0.04	$	0.13	$	(0.15)	$	0.28
Income from discontinued operations				0.01				0.02
Net income (loss) attributable to common stockholders	$	0.04	$	0.14	$	(0.15)	$	0.30
Earnings per common share diluted:								
Income (loss) from continuing operations (net of preferred stock dividends)	$	0.04	$	0.12	$	(0.14)	$	0.27
Income from discontinued operations				0.01				0.02
Net income (loss) attributable to common stockholders	$	0.04	$	0.13	$	(0.14)	$	0.29
Weighted average common shares outstanding		7,611		7,745		7,604		7,728
Weighted average common shares and common share equivalents outstanding		7,710		8,029		7,734		8,052
Dividends declared per common share	$	0.25	$	0.25	$	0.50	$	0.50

See Notes to Condensed Consolidated Financial Statement

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AMERICAN LAND LEASE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY

(in thousands)

(unaudited)

	Preferred Stock		Common Stock		Additional Paid-In Capital	Dividends In Excess of Accumulated Earnings	Treasury Stock	Total Stockholders Equity
	Shares	Amount	Shares	Amount				
BALANCES DECEMBER 31, 2007	1,000	$ 25,000	9,485	$ 95	$ 293,821	$ (148,749)	$ (31,163)	$ 139,004
Exercise of options			86	1	602			603
Vesting of restricted stock			15					
Equity compensation granted to the Board of Directors			9		175			175
Purchase of treasury stock							(756)	(756)
Stock-based compensation					668			668
Net loss						(145)		(145)
Dividends paid preferred stock						(969)		(969)
Dividends paid common stock						(3,947)		(3,947)
BALANCES JUNE 30, 2008	1,000	$ 25,000	9,595	$ 96	$ 295,266	$ (153,810)	$ (31,919)	$ 134,633

See Notes to Condensed Consolidated Financial Statements

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AMERICAN LAND LEASE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net (loss) income	$ (145)	$ 3,274
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	3,320	3,030
Loss on early debt retirement	1,987	
Revenue recognized related to acquired lease obligations	(142)	(263)
Stock-based compensation	648	611
Minority interest in Operating Partnership	(19)	399
Minority interest in Operating Partnership attributable to discontinued operations		20
Decrease in inventory	4,243	1,796
Net change in operating assets and liabilities	(1,038)	552
Net cash provided by operating activities	8,854	9,419
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to real estate, including development	(4,741)	(11,762)
Capitalized interest	(4,456)	(4,423)
Capital replacements	(447)	(727)
Additions to fixed assets other than real estate classified as other assets	(89)	(246)
Construction loan advances	(2,227)	(89)
Proceeds from notes receivable	237	266
Net cash used in investing activities	(11,723)	(16,981)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from secured credit facilities	48,795	55,030
Payments on secured credit facilities	(58,508)	(45,076)
Proceeds from secured notes payable	36,955	4,580
Principal payments on secured notes payable	(17,295)	(1,471)
Early debt retirement	(1,874)	
Payments of deferred financing costs		(73)
Payments to escrow funds	(281)	(172)
Collections of escrowed funds	243	92
Proceeds from stock options exercised	603	797
Purchase of treasury stock	(756)	(627)
Payments of common stock dividends	(3,947)	(3,994)
Payments of preferred stock dividends	(969)	(969)
Distributions to minority interest in Operating Partnership	(496)	(500)
Net cash provided by financing activities	2,470	7,617
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(399)	55
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	541	253

CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 142	$ 308

See Notes to Condensed Consolidated Financial Statements

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AMERICAN LAND LEASE, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2008

(unaudited)

A. The Company

American Land Lease, Inc. (ANL) is a Delaware corporation that owns home sites leased to owners of homes situated on the leased land and operates the communities composed of these homes. ANL has elected to be taxed as a real estate investment trust (REIT). ANL s preferred stock, par value $.01 per share, is listed on the New York Stock Exchange (NYSE) under the symbol ANLPRA. ANL s common stock, par value $.01 per share, is listed on the NYSE under the symbol ANL. In May 1997, ANL contributed its net assets to Asset Investors Operating Partnership, L.P. (the Operating Partnership) in exchange for the sole general partner interest in the Operating Partnership and substantially all of the Operating Partnership s initial capital. Except as the context requires, we, our, us, ANL and the Company refer to American Land Lease, In Operating Partnership and all majority-owned subsidiaries.

Interests in the Operating Partnership held by limited partners other than ANL are referred to as OP Units. The Operating Partnership s income is allocated to holders of OP Units based on the weighted average number of OP Units outstanding during the period. The holders of the OP Units receive distributions, prorated from the date of issuance, in an amount equivalent to the dividends paid, if any, to holders of ANL s common stock. After holding the OP Units for one year, limited partners generally have the right to redeem their OP Units for cash. Notwithstanding that right, the Operating Partnership may elect to acquire some or all of the OP Units tendered for redemption in exchange for shares of ANL s common stock in lieu of cash. At June 30, 2008, the Operating Partnership had approximately 993,000 OP Units outstanding, excluding those owned by ANL, and ANL owned 88% of the Operating Partnership.

As of June 30, 2008, based on total home sites, 72% of the Company s portfolio of residential land lease communities is located in Florida, 24% in Arizona and 4% in Alabama.

B. Presentation of Financial Statements

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X under the Securities Exchange Act of 1934, as amended. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included and are of a normal recurring nature. Operating results for the three and six months ended June 30, 2008 are not necessarily indicative of the results that may be expected for the year ending December 31, 2008.

The condensed consolidated balance sheet at December 31, 2007 has been derived from the audited financial statements at that date but does not include all of the information and notes required by GAAP.

For further information, refer to the statements and notes thereto included in ANL s Annual Report on Form 10-K for the year ended December 31, 2007.

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C. Summary of Significant Accounting Policies
Principles of Consolidation

The consolidated financial statements include the accounts of ANL, the Operating Partnership and all majority owned subsidiaries. The minority interest in the Operating Partnership represents the OP Units that are redeemable at the option of the holder. All significant intercompany balances and transactions have been eliminated in consolidation.

The Company applies Financial Accounting Standards Board (FASB) Interpretation No. 46, *Consolidation of Variable Interest Entities (revised December 2003), an interpretation of ARB No. 51* (FIN 46R). The objective of FIN 46R is to provide guidance on how to identify a variable interest entity (VIE) and determine when the assets, liabilities, non-controlling interests, and results of operations of a VIE need to be included in a company s consolidated financial statements. A company that holds variable interests in an entity will need to consolidate such entity if the company absorbs a majority of the entity s expected losses or receives a majority of the entity s expected residual returns if they occur, or both (i.e., the primary beneficiary).

Real Estate and Depreciation

The Company capitalizes direct costs associated with the acquisition of consolidated properties as a cost of the assets acquired, and such direct costs are depreciated over the estimated useful lives of the related assets. In accordance with FASB Statement of Financial Accounting Standards (SFAS) No. 141, *Business Combinations* (SFAS 141), the Company allocates the purchase price of real estate to land, land improvements, buildings, furniture, fixtures, equipment and intangibles, such as the value of above and below market leases and origination costs associated with the in-place leases. In order to allocate purchase price on these various components, the Company performs the following procedures for properties acquired:

1. Determine the as-if vacant fair value of the physical property acquired;

2. Allocate the as-if vacant fair value among land, land improvements, buildings, (based on real estate valuation techniques), furniture, fixtures and equipment; and

3. Compute the difference between the purchase price of the property and the as-if vacant fair value and allocate such difference to leases in-place, which will represent the total intangible assets or liabilities. The fair value of the leases in-place are comprised of:

   a. The value of the above and/or below market leases in-place. Above-market and below-market in-place lease values are computed based on the difference between (i) the contractual amounts to be paid pursuant to the in-place leases and (ii) management s estimate of fair market lease rates and effective lease terms for the corresponding in-place leases, measured over a period equal to the estimated remaining effective terms of the leases.

   b. Avoided leasing commissions and other costs that were incurred to execute leases.

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c. The value associated with lost rents during the absorption period (estimates of lost rental revenue during the expected lease-up periods based on current market demand).

The values of the above and below market leases are amortized and recorded as either an increase (in the case of below market leases) or a decrease (in the case of above market leases) to rental income over the estimated remaining expected terms of the associated leases (including fixed rate renewal periods for below market leases). Amortization expense is recorded over the expected remaining terms of the associated leases for the values associated with avoided leasing commissions, other costs that were incurred to execute leases and the value associated with lost rents during the absorption period. If a resident vacates a home site prior to the effective term of the lease and no rental payments are being made on the lease, any unamortized balance of the related intangible will be written off.

Rental properties are recorded at cost less accumulated depreciation, unless considered impaired. Significant renovations and improvements, which improve or extend the useful life of an asset, are capitalized and depreciated using the straight-line method over the remaining estimated life. In addition, the Company capitalizes direct and indirect costs (including interest, taxes and other costs) in connection with the development of additional home sites within its residential land lease communities. Maintenance, repairs and minor improvements are expensed as incurred.

Interest incurred relating to the development of communities is capitalized during the development period. The Company s strategy is to master plan, develop and build substantially all of the home sites in its communities. Accordingly, substantially all projects excluding finished lots where the home is available for occupancy, are undergoing development. The Company capitalized interest of approximately $2,194,000 and $2,248,000 for the three months ended June 30, 2008 and 2007, and $4,456,000 and $4,423,000 for the six months ended June 30, 2008 and 2007, respectively.

If events or circumstances indicate that the carrying amount of a property may be impaired, the Company will make an assessment of its recoverability by estimating the future undiscounted cash flows, excluding interest charges, of the property. In the event the property is under development, the estimate of future cash flows includes all future expenditures necessary to develop the property. If the carrying amount exceeds the aggregate future cash flows, the Company would recognize an impairment loss to the extent the carrying amount exceeds the fair value of the property. There were no impairment losses recognized for the six months ended June 30, 2008 and 2007.

Depreciation is computed using the straight-line method over an estimated useful life of 5 to 75 years for land improvements, 5 to 50 years for buildings and 5 to 15 years for furniture and other equipment, all of which are judgmental determinations. These determinations may prove to be different than the actual life of any individual asset.

Cash Equivalents

The Company considers highly liquid investments with an original maturity of three months or less to be cash equivalents.

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Inventory

The Company, through a taxable subsidiary corporation, maintains an inventory of manufactured homes situated within its residential land lease communities. Carrying amounts for inventory are determined on a specific identification basis and are stated at the lower of cost or estimated market value. If actual market conditions are less favorable than those projected by management and the market value of our inventory is lower then estimated by management, inventory write-downs may be required that could have a significant impact on the Company s results of operations and cash flows. As of June 30, 2008, $12,370,000 of the Company s total inventory investment of $15,841,000 was older than one year. The Company recorded charges of approximately $256,000 and $68,000 for the three months ended June 30, 2008 and 2007, and $365,000 and $200,000 for the six months ended June 30, 2008 and 2007, respectively, to adjust inventory carrying amounts to market value.

Revenue Recognition

The Company generates income from the rental of home sites. The leases entered into by residents for the rental of home sites are generally for terms of one year, and the rental revenues associated with the leases are recognized when earned and due from residents.

The Company, through a taxable subsidiary corporation, generates income from memberships, daily green fees, cart rentals and merchandise sales at golf courses located within its communities. Revenues associated with the activities of the golf courses are recognized when earned and received by the Company.

The Company, through a taxable subsidiary corporation, generates income from the sale of homes situated on home sites owned by the Company. Sales of homes by the Company are recorded upon the closing of the home sale transaction and title passing to the purchaser.

Deferred Financing Costs

Fees and costs incurred in obtaining financing are capitalized. Such costs are amortized over the terms of the related loan agreements using the effective interest method and are charged to interest expense.

Advertising Costs

Costs of advertising are expensed the first time the advertising takes place. Direct response advertising conducted by the Company during the periods was expensed as incurred, as the Company could not define the expected period of future benefits. Advertising expenses were $203,000 and $575,000 for the three months ended June 30, 2008 and 2007, respectively, and $552,000 and $1,134,000 for the six months ended June 30, 2008 and 2007, respectively, and are included within golf course operating expenses and selling and marketing expenses in the consolidated statements of operations.

Income Taxes

ANL has elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended. To qualify as a REIT, ANL must meet a number of organizational and operational requirements, including income, asset, and stockholder requirements, and a requirement that, in general, it must distribute currently at least 90% of its adjusted taxable income to its stockholders. It is management s current intention to adhere to these requirements and maintain ANL s REIT status. As a REIT, ANL generally will not be subject to corporate level federal income tax on taxable income that it distributes currently to its stockholders, by virtue of a deduction for dividends paid. If ANL fails to qualify as a REIT in any taxable year, it will be subject to federal income taxes at regular corporate rates (including any applicable alternative minimum tax) and, unless entitled to relief under certain statutory provisions, may not be able to qualify as a REIT for four subsequent taxable years. Even if ANL qualifies for taxation as a REIT, ANL may be subject to certain state and local taxes on its income and property, and to federal income and excise taxes and penalties, including taxes on ANL s undistributed taxable income. In addition, taxable income from non-REIT activities conducted through ANL s taxable subsidiaries is subject to federal, state, and local income taxes.

The Company files its tax returns as prescribed by the tax laws of the jurisdictions in which it operates. The Company s federal and state income tax returns for the years ended December 31, 2004, and subsequent years are currently subject to examination by the Internal Revenue Service or other taxing authorities. The Company recognizes accrued interest related to unrecognized tax benefits as a component of interest expense and penalties related to unrecognized tax benefits as a component of general and administrative expenses. In March 2008, the Company was notified by the Internal Revenue Service that it intends to examine the 2005 federal tax return for Asset Investors Operating Partnership. The Internal Revenue Service examined the 2005 federal tax return for Asset Investors Operating Partnership and concluded that no change was necessary to the return and accepted the return as filed.

Earnings Per Share

Basic earnings per share are based upon the weighted-average number of shares of common stock outstanding during each period. Diluted earnings per share reflect the effect of dilutive, unexercised stock options, both vested and unvested, and unvested restricted stock of 99,000 and 284,000 shares for the three months ended June 30, 2008 and 2007, respectively, and 130,000 and 324,000 shares for the six months ended June 30, 2008 and 2007, respectively. Vested and unvested stock options totaling 453,000 and 148,000 shares for the three months ended June 30, 2008 and 2007, respectively, and 448,000 and 148,000 shares for the six months ended June 30, 2008 and 2007, respectively, were excluded from diluted earnings as their effect was anti-dilutive.

Stock-based Compensation

The Company used the Black-Scholes-Merton formula to estimate the fair value of stock options, used the closing stock price at date of grant for time-based restricted stock and used a Monte Carlo model to estimate the fair value of market-based restricted stock for the six months ended June 30, 2008 and 2007. Stock-based compensation is reported in selling and marketing expenses and general and administrative expenses. The Company recorded stock-based compensation expense of $364,000 and $307,000 for the three months ended June 30, 2008 and 2007, respectively, and $648,000 and $611,000 for the six months ended June 30, 2008 and 2007, respectively.

Treasury Stock

On October 17, 2000, the Board of Directors authorized the Company to repurchase up to 2,000,000 shares of the outstanding common stock. The timing of stock purchases is at the discretion of

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management. The Company purchased 0 and 0 shares for the three months ended June 30, 2008 and 2007, respectively, and 29,000 and 27,000 shares for the six months ended June 30, 2008 and 2007, respectively. The Company has repurchased approximately 812,000 shares as of June 30, 2008 pursuant to this authorization.

Depreciation of Personal Property

Depreciation of personal property is reported in property operating expenses, selling and marketing expenses, or general and administrative expenses, based upon the use of the associated asset. The Company recorded depreciation expense related to personal property of $111,000 and $99,000 for the three months ended June 30, 2008 and 2007, respectively, and $212,000 and $192,000, for the six months ended June 30, 2008 and 2007, respectively. Depreciation is computed using the straight-line method over an estimated useful life of 5 to 15 years for furniture and other equipment, all of which are judgmental determinations. These determinations may prove to be different than the actual life of any individual asset.

Statements of Cash Flows

The Company considers cash maintained in bank accounts, money market funds and highly liquid investments with an initial maturity of three months or less to be cash equivalents.

Non-cash financing activities for the period ended June 30, 2008 and 2007 were as follows:

	2008	**2007**
Issuance of common stock for:		
Services by directors	$ 175,000	$ 194,000

Fair Value of Financial Instruments

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurement* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS 157 is effective for financial assets and financial liabilities for fiscal years beginning after November 15, 2007. In February 2008, the FASB issued Staff Position No. 157-2, *Effective Date of FASB Statement No. 157*, which deferred the effective date of SFAS 157 for all nonfinancial assets and nonfinancial liabilities to fiscal years beginning after November 2008.

The implementation of SFAS 157 for financial assets and financial liabilities, effective January 1, 2008, did not have a material impact on the Company s consolidated financial position and results of operations. The Company is currently assessing the impact of SFAS 157 for nonfinancial assets and nonfinancial liabilities on its consolidated financial position and results of operations.

The estimated fair value of the Company s secured notes payable was $260,475,000 at June 30, 2008 as compared to the carrying value of $259,630,000 at June 30, 2008.

The aggregate fair value of cash and cash equivalents, receivables, accounts payable and accrued liabilities as of June 30, 2008 approximates their carrying value due to their relatively short-term nature.

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Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Reclassifications

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (SFAS 144), certain reclassifications have been made in the 2007 consolidated financial statements to present the operations of one community as discontinued operations for all periods presented. Such reclassifications have no material effect on the amounts as originally presented.

Comprehensive Income

SFAS No. 130, *Reporting Comprehensive Income*, requires all components of comprehensive income be reported in the consolidated financial statements in the period in which they are recognized. For all periods reported, the Company s comprehensive income is equal to its net income reported in the accompanying consolidated statements of operations.

D. Real Estate

Real estate at June 30, 2008 and December 31, 2007 is as follows (in thousands):

	June 30, 2008	December 31, 2007
Land	$ 92,900	$ 92,664
Land improvements and buildings	347,765	338,695
	440,665	431,359
Less accumulated depreciation	(34,145)	(31,842)
Real estate, net	$ 406,520	$ 399,517

The Company s real estate investment consists of land, land improvements and buildings. Buildings consist primarily of clubhouses at its residential land lease communities maintained as amenities for resident use. A majority of the Company s investment in land improvements consists of long-lived assets such as lateral infrastructure at its residential land lease communities including sanitary sewer and storm water collection systems, potable water supply systems, roads and walkways. The balance of land improvements consists of assets with shorter lives such as marinas, fencing, swimming pools, spas, shuffleboard courts, tennis courts and other resident amenities. Depreciation is computed using the straight-line method over an estimated useful life of 5 to 75 years for land improvements and 5 to 50 years for buildings.

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E. Secured Notes Payable

The following table summarizes the Company s secured notes payable (in thousands):

	June 30, 2008	December 31, 2007
Fixed rate, ranging from 7.86% to 7.92%, fully amortizing, non-recourse notes maturing in 2020	$ 7,659	$ 9,882
Fixed rate, ranging from 5.48% to 7.17%, partially amortizing, non-recourse notes maturing at various dates from 2013 through 2021	229,865	207,982
Variable rate, at the three-month LIBOR rate plus 115 to 175 basis points, interest only non-recourse notes maturing at various dates from 2011 through 2012	22,106	22,106
	$ 259,630	$ 239,970

F. Secured Credit Facilities

The Company has a revolving line of credit with a bank with a total commitment of $16,000,000 that bears interest at 175 basis points over the one-month LIBOR rate (4.2% at June 30, 2008 and 6.6% at December 31, 2007). The line of credit is secured by real property and improvements located in St. Lucie, Lake, and Pasco County, Florida and Maricopa County, Arizona with a net book value of $44,067,000. The revolving line of credit matures December 31, 2008. At June 30, 2008, $4,600,000 was outstanding and $11,400,000 was not drawn under the revolving line of credit. The availability of funds to the Company under the line of credit is subject to certain borrowing base and other customary restrictions, including compliance with financial and other covenants thereunder. Based on the application of the borrowing base calculation, as of June 30, 2008, $8,392,000 was available to the Company. The line of credit also includes certain financial covenants that require the Company to maintain an adjusted tangible net worth (as defined by the lender) of $150,000,000 and to maintain a debt to adjusted tangible net worth ratio of not more than 1.75 to 1.0, among others. The Company believes it was in compliance with all financial covenant requirements at June 30, 2008.

The Company has a floor plan line of credit with a floor plan lender providing a committed credit facility of $35,000,000 with a variable interest rate linked to the lender s prime rate, with a floor of 5.25%, plus 25 basis points (5.5% at June 30, 2008 and 7.8% at December 31, 2007). Individual advances mature the earlier of 1,080 days or upon sale of the home to a third party. This floor plan line of credit is secured by inventory located in the Company s residential land lease communities with a carrying value of approximately $14,330,000. At June 30, 2008, approximately $16,619,000 was outstanding, of which $2,250,000 was recourse to the Company, and approximately $18,381,000 was available under the floor plan credit facility. The financial covenants of the floor plan line of credit require the Company to maintain an adjusted tangible net worth (as defined by the lender) of $150,000,000 and to maintain a debt to adjusted tangible net worth ratio of not more than 1.75 to 1.0, among others. The floor plan lender s commitment to fund future inventory purchases expires in September 2009. The Company believes it was in compliance with all financial covenant requirements at June 30, 2008.

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G. Commitments and Contingencies

Legal Contingencies

The Company is party to various legal actions resulting from its operating activities. These actions are routine litigation and administrative proceedings arising in the ordinary course of business, some of which are covered by liability insurance, and none of which are expected to have a material adverse effect on the consolidated financial condition or results of operations of the Company and its subsidiaries taken as a whole. It is possible, however, that future results of operations for any particular quarterly or annual period could be materially affected by changes in assumptions and effectiveness of strategies, related to these proceedings.

Commitments

In the ordinary course of business, the Company has entered into various construction contracts with third parties to develop subdivisions within the Company s existing portfolio of residential land lease communities. The unpaid balance of these contracts remaining at June 30, 2008 is approximately $1,375,000.

During 2007, the Company issued a construction loan to a development company in Arizona. The maximum aggregate amount of advances available under the construction loan is $8,080,000, subject to certain inventory level restrictions provided for in the loan documents that limit the aggregate amount of advances outstanding at any given time. The proceeds of the loan are to be used exclusively to develop a community for the Company in Mesa, Arizona. At June 30, 2008, the application of the inventory restriction limits the additional funds available to the development company to approximately $4,052,000. At June 30, 2008, approximately $1,082,000 was available under the construction loan.

H. Segment Reporting

The Company has two reportable segments: real estate (ownership of land leases, land development, investment acquisition and disposition) and home sales (sale of homes, both new and used, to be sited on land owned by the Company). The real estate segment consists of residential land lease communities that generate rental and other property related income through the leasing of land to residents that are unaffiliated with the Company. The home sales segment sells manufactured homes to customers that are unrelated to the Company. The homes sold by the home sales segment are situated on land within the Company s portfolio of rental property. The customers of the home sales business become residents of the Company s real estate segment coincident with the sale of a home, at which time the customer enters into a lease with the real estate segment. The chief operating decision maker assesses the performance of the real estate segment using, among other measures, net operating income excluding depreciation as a key measurement of segment profit or loss. The chief operating decision maker assesses the performance of the home sales segment using, among other measures, contribution margin, excluding allocated corporate expenses as the best measure of the segments performance. Segment operating income is generally defined as segment revenues less direct segment operating expenses.

Non-segment revenue used to reconcile total revenue consists primarily of interest income and other income. Non-segment assets used to reconcile to total assets include cash and cash equivalents, cash in escrows, accounts receivable, prepaid expenses, investments, deferred charges and other assets.

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Overhead expenses, such as administrative expenses, are allocated to each segment based upon management s best estimate of the resources utilized in the management and operations of each segment. The accounting policies of the segments are the same as those described in Note C.

The revenues, net income (loss), and assets for each of the reportable segments are summarized in the following tables for the three and six months ended June 30, 2008 and June 30, 2007 (in thousands).

	Three months ended June 30, 2008			
	Real Estate	Home Sales	Corporate, (not allocated to segments)	Consolidated
Rental and other property revenues, net	$ 9,950	$	$	$ 9,950
Home sales revenues		3,564		3,564
Total revenues	9,950	3,564		13,514
Net operating income gross profit for real estate segment	6,446			6,446
Home sales contribution margin		(792)		(792)
Adjustments to arrive at net income:				
Depreciation	(1,351)			(1,351)
General and administrative expenses	(904)	(324)	(5)	(1,233)
Interest expense			(2,198)	(2,198)
Interest and other income			58	58
Minority interest in earnings			(108)	(108)
Net income (loss)	$ 4,191	$ (1,116)	$ (2,253)	$ 822
Assets	$ 412,419	$ 23,826	$ 4,257	$ 440,502
Capital additions to:				
Real estate	$ 4,194	$	$	