PENNSYLVANIA REAL ESTATE INVESTMENT TRUST
Form 10-Q
November 07, 2007
Table of Contents

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 September 30, 2007

or

¨ Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from ______ to ______

Commission File Number: 1-6300

PENNSYLVANIA REAL ESTATE INVESTMENT TRUST

(Exact name of Registrant as specified in its charter)

Pennsylvania	**23-6216339**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
200 South Broad Street	
Philadelphia, PA	**19102**

(Address of principal executive offices) **(Zip Code)**

Registrant s telephone number, including area code (215) 875-0700

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 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.

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

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Common shares of beneficial interest, $1.00 par value per share, outstanding at November 1, 2007: 38,952,042

Table of Contents

PENNSYLVANIA REAL ESTATE INVESTMENT TRUST

CONTENTS

Table of Contents

PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

PENNSYLVANIA REAL ESTATE INVESTMENT TRUST

CONSOLIDATED BALANCE SHEETS

(in thousands, except per share amounts)

(Unaudited)

	September 30, 2007	December 31, 2006
ASSETS:		
INVESTMENTS IN REAL ESTATE, at cost:		
Operating properties	$ 2,960,023	$ 2,909,862
Construction in progress	320,494	216,892
Land held for development	5,616	5,616
Total investments in real estate	3,286,133	3,132,370
Accumulated depreciation	(375,013)	(306,893)
Net investments in real estate	2,911,120	2,825,477
INVESTMENTS IN PARTNERSHIPS, at equity:	36,895	38,621
OTHER ASSETS:		
Cash and cash equivalents	23,548	15,808
Rents and other receivables (net of allowance for doubtful accounts of $11,550 and $11,120 at September 30, 2007 and December 31, 2006, respectively)	38,812	46,065
Intangible assets (net of accumulated amortization of $129,413 and $108,545 at September 30, 2007 and December 31, 2006, respectively)	112,519	139,117
Deferred costs and other assets	99,916	79,120
Assets held for sale		1,401
Total assets	$ 3,222,810	$ 3,145,609
LIABILITIES:		
Mortgage notes payable	$ 1,649,278	$ 1,572,908
Debt premium on mortgage notes payable	16,930	26,663
Exchangeable senior notes	287,500	
Credit Facility	245,000	332,000
Corporate notes payable	1,148	1,148
Tenants deposits and deferred rents	12,568	12,098
Distributions in excess of partnership investments	55,215	63,439
Accrued expenses and other liabilities	113,674	93,656
Liabilities related to assets held for sale		34
Total liabilities	2,381,313	2,101,946
MINORITY INTEREST:	66,979	114,363

COMMITMENTS AND CONTINGENCIES (Note 9)		
SHAREHOLDERS EQUITY:		
Shares of beneficial interest, $1.00 par value per share; 100,000 shares authorized; issued and outstanding 38,664 shares at September 30, 2007 and 36,947 shares at December 31, 2006, respectively	38,664	36,947
Non-convertible senior preferred shares, 11% cumulative, $.01 par value per share; 2,475 shares authorized, issued and outstanding at December 31, 2006		25
Capital contributed in excess of par	805,811	917,322
Accumulated other comprehensive income	10,055	7,893
Distributions in excess of net income	(80,012)	(32,887)
Total shareholders equity	774,518	929,300
Total liabilities, minority interest and shareholders equity	$ 3,222,810	$ 3,145,609

See accompanying notes to the unaudited consolidated financial statements.

1

Table of Contents

PENNSYLVANIA REAL ESTATE INVESTMENT TRUST

CONSOLIDATED STATEMENTS OF INCOME

(in thousands of dollars)

(Unaudited)

	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
REVENUE:				
Real estate revenue:				
Base rent	$ 71,547	$ 70,644	$ 213,300	$ 210,909
Expense reimbursements	33,369	33,951	101,028	99,544
Percentage rent	1,289	1,433	4,922	5,196
Lease termination revenue	690	440	1,408	2,583
Other real estate revenue	3,985	4,518	11,638	12,704
Total real estate revenue	110,880	110,986	332,296	330,936
Management company revenue	854	545	1,827	1,832
Interest and other income	535	566	2,323	1,452
Total revenue	112,269	112,097	336,446	334,220
EXPENSES:				
Property operating expenses:				
CAM and real estate taxes	(31,620)	(31,408)	(95,116)	(92,429)
Utilities	(6,886)	(6,886)	(19,055)	(17,965)
Other operating expenses	(5,968)	(6,759)	(17,263)	(19,214)
Total property operating expenses	(44,474)	(45,053)	(131,434)	(129,608)
Depreciation and amortization	(32,743)	(30,807)	(96,970)	(91,421)
Other expenses:				
General and administrative expenses	(9,888)	(9,567)	(31,314)	(29,817)
Executive separation				(3,985)
Income taxes and other	(109)	(142)	(520)	(383)
Total other expenses	(9,997)	(9,709)	(31,834)	(34,185)
Interest expense	(24,866)	(24,041)	(72,338)	(72,319)
Total expenses	(112,080)	(109,610)	(332,576)	(327,533)
Income before equity in income of partnerships, gains on sales of interests in real estate, minority interest and discontinued operations	189	2,487	3,870	6,687
Equity in income of partnerships	1,148	1,044	3,272	4,075
Gains on sales of interests in real estate			579	
Gains on sales of non-operating real estate	247	166	1,731	381
Income before minority interest and discontinued operations	1,584	3,697	9,452	11,143
Minority interest	(103)	(395)	(884)	(1,221)
Income from continuing operations	1,481	3,302	8,568	9,922

Income (loss) from discontinued operations:				
Operating results from discontinued operations	19	(31)	(118)	(2,386)
Gain on sale of discontinued operations		1,414	6,699	1,414
Minority interest	(1)	(141)	(691)	98
Income (loss) from discontinued operations	18	1,242	5,890	(874)
Net income	1,499	4,544	14,458	9,048
Redemption of preferred shares	13,347		13,347	
Dividends on preferred shares	(1,134)	(3,403)	(7,941)	(10,209)
Net income available (loss allocable) to common shareholders	$ 13,712	$ 1,141	$ 19,864	$ (1,161)

See accompanying notes to the unaudited consolidated financial statements.

Table of Contents

PENNSYLVANIA REAL ESTATE INVESTMENT TRUST

CONSOLIDATED STATEMENTS OF INCOME (CONTINUED)

(in thousands, except per share amounts)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
EARNINGS (LOSS) PER SHARE:	**2007**	**2006**	**2007**	**2006**
Income from continuing operations	$ 1,481	$ 3,302	$ 8,568	$ 9,922
Redemption of preferred shares	13,347		13,347	
Dividends on preferred shares	(1,134)	(3,403)	(7,941)	(10,209)
Income (loss) from continuing operations allocable to common shareholders	13,694	(101)	13,974	(287)
Dividends on unvested restricted shares	(272)	(247)	(815)	(796)
Income (loss) from continuing operations used to calculate earnings per share	$ 13,422	$ (348)	$ 13,159	$ (1,083)
Income (loss) from discontinued operations used to calculate earnings per share	$ 18	$ 1,242	$ 5,890	$ (874)
Basic earnings (loss) per share				
Income (loss) from continuing operations	$ 0.35	$ (0.01)	$ 0.35	$ (0.03)
Income (loss) from discontinued operations	0.00	0.03	0.16	(0.02)
	$ 0.35	$ 0.02	$ 0.51	$ (0.05)
Diluted earnings (loss) per share				
Income (loss) from continuing operations	$ 0.35	$ (0.01)	$ 0.35	$ (0.03)
Income (loss) from discontinued operations	0.00	0.03	0.16	(0.02)
	$ 0.35	$ 0.02	$ 0.51	$ (0.05)
Weighted average shares outstanding-basic	38,181	36,282	37,219	36,189
Effect of common shares equivalents	295		363	
Weighted average shares outstanding-diluted	38,476	36,282(1)	37,582	36,189(1)

(1) For the three and nine month periods ended September 30, 2006, there are net losses allocable to common shareholders from continuing operations, so the effect of common share equivalents is excluded from the calculation of diluted income (loss) per share for these periods because it would be antidilutive.

See accompanying notes to the unaudited consolidated financial statements.

Table of Contents

PENNSYLVANIA REAL ESTATE INVESTMENT TRUST

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands of dollars)

(Unaudited)

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Cash Flows from Operating Activities:		
Net income	$ 14,458	$ 9,048
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	73,433	68,132
Amortization	15,865	17,750
Straight-line rent adjustments	(1,515)	(2,119)
Provision for doubtful accounts	2,083	2,669
Amortization of deferred compensation	5,208	4,657
Minority interest	1,575	1,123
Gains on sales of interests in real estate	(9,009)	(1,794)
Change in assets and liabilities:		
Net change in other assets	(1,238)	1,160
Net change in other liabilities	194	15,189
Net cash provided by operating activities	101,054	115,815
Cash Flows from Investing Activities:		
Investments in consolidated real estate acquisitions, net of cash acquired	(11,280)	(34,969)
Investments in consolidated real estate improvements	(13,589)	(25.006)
Additions to construction in progress	(144,742)	(108,950)
Investments in partnerships	(9,497)	(1,519)
Decrease (increase) in cash escrows	5,049	(961)
Capitalized leasing costs	(3,502)	(3,458)
Additions to leasehold improvements	(811)	(570)
Cash distributions from partnerships in excess of equity in income	2,998	55,454
Cash proceeds from sales of consolidated real estate investments	31,486	9,039
Net cash used in investing activities	(143,888)	(110,940)
Cash Flows from Financing Activities:		
Proceeds from sale of exchangeable senior notes	281,031	
Proceeds from mortgage notes payable	150,000	246,500
Repayment of mortgage notes payable	(56,663)	
Net repayment of Credit Facility	(87,000)	(65,500)
Repayment of corporate notes payable		(94,400)
Principal installments on mortgage notes payable	(16,967)	(17,083)
Cash proceeds from settlement of interest rate swap agreements	4,069	
Payment of deferred financing costs	(3,511)	(1,358)
Purchase of capped calls	(12,578)	
Shares of beneficial interest issued	13,845	4,940
Shares of beneficial interest repurchased	(12,427)	(2,545)
Operating partnership units redeemed	(78)	(352)
Redemption of preferred shares	(129,955)	

Distributions paid to common shareholders	(64,271)	(62,789)
Distributions paid to preferred shareholders	(8,659)	(10,209)
Distributions paid to operating partnership unit holders and minority partners	(6,262)	(6,587)
Net cash provided by (used in) financing activities	50,574	(9,383)
Net change in cash and cash equivalents	7,740	(4,508)
Cash and cash equivalents, beginning of period	15,808	21,642
Cash and cash equivalents, end of period	$ 23,548	$ 17,134

See accompanying notes to the unaudited consolidated financial statements.

Table of Contents

PENNSYLVANIA REAL ESTATE INVESTMENT TRUST

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2007

(Unaudited)

1. BASIS OF PRESENTATION:

Pennsylvania Real Estate Investment Trust (PREIT or the Company) prepared the accompanying consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the included disclosures are adequate to make the information presented not misleading. The consolidated financial statements should be read in conjunction with the audited financial statements and the notes thereto included in PREIT s Annual Report on Form 10-K filed on March 1, 2007 for the year ended December 31, 2006, and as revised by PREIT s Current Report on Form 8-K filed on July 16, 2007 that was filed to reflect the operations of Schuylkill Mall as discontinued operations and the reclassification of P&S Office Building to continuing operations. In management s opinion, all adjustments, consisting only of normal recurring adjustments, necessary to present fairly the consolidated financial position of the Company and its subsidiaries and the consolidated results of its operations and its cash flows are included. The results of operations for the interim periods presented are not necessarily indicative of the results for the full year.

Pennsylvania Real Estate Investment Trust, a Pennsylvania business trust founded in 1960 and one of the first equity real estate investment trusts (REITs) in the United States, has a primary investment focus on retail shopping malls and power and strip centers located in the Mid-Atlantic region or in the eastern half of the United States. As of September 30, 2007, the Company s portfolio consisted of a total of 55 properties. The Company s retail portfolio contains 49 properties in 13 states and includes 38 shopping malls and 11 power and strip centers. The ground-up development portion of the Company s portfolio contains six properties in four states, with three classified as power centers, two classified as mixed use (a combination of retail and other uses) and one classified as other.

The Company holds its interest in its portfolio of properties through its operating partnership, PREIT Associates, L.P. (the Operating Partnership). The Company is the sole general partner of the Operating Partnership and, as of September 30, 2007, the Company held a 93.5% interest in the Operating Partnership, and consolidates it for reporting purposes. The presentation of consolidated financial statements does not itself imply that the assets of any consolidated entity (including any special-purpose entity formed for a particular project) are available to pay the liabilities of any other consolidated entity, or that the liabilities of any consolidated entity (including any special-purpose entity formed for a particular project) are obligations of any other consolidated entity.

Pursuant to the terms of the partnership agreement of the Operating Partnership, each of the limited partners has the right to redeem his/her units of limited partnership interest in the Operating Partnership (OP Units) for cash or, at the election of the Company, the Company may acquire such OP Units for shares of the Company on a one-for-one basis, in some cases beginning one year following the respective issue date of the OP Units and in other cases immediately.

The Company provides its management, leasing and real estate development services through two companies: PREIT Services, LLC (PREIT Services), which generally develops and manages properties that the Company consolidates for financial reporting purposes, and PREIT-RUBIN, Inc. (PRI), which generally develops and manages properties for third parties as well as properties that the Company does not consolidate for financial reporting purposes, including properties owned by partnerships in which the Company owns an interest. PREIT Services and PRI are consolidated. Because PRI is a taxable REIT subsidiary as defined by federal tax laws, it is capable of offering a broad range of services to tenants without jeopardizing the Company s continued qualification as a real estate investment trust under federal tax law.

Certain prior period amounts have been reclassified to conform with the current period presentation.

2. RECENT ACCOUNTING PRONOUNCEMENTS:

SFAS No. 159

In February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS No. 159). SFAS No. 159 expands opportunities to use fair value measurement in financial reporting and permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Company has not determined whether the adoption of SFAS No. 159 will have any material effect on the Company s financial statements.

Table of Contents

SFAS No. 157

In September 2006, FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 establishes a new definition of fair value, provides guidance on how to measure fair value and establishes new disclosure requirements of assets and liabilities at their fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. The Company has not determined whether the adoption of SFAS No. 157 will have any material effect on the Company s financial statements.

FIN 48

In June 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). FIN 48 addresses the recognition and measurement of tax-based benefits on the probability that they will be realized. FIN 48 is effective for fiscal years beginning after December 15, 2006. The adoption of FIN 48 had no material impact on the Company s financial statements.

The Company, or its subsidiaries, file income tax returns in the U.S. federal jurisdiction and in various state and local jurisdictions. The Company s open tax years generally include tax years 2003 to 2006 as of the date of adoption.

3. REAL ESTATE ACTIVITIES:

Investments in real estate as of September 30, 2007 and December 31, 2006 were comprised of the following:

(in thousands of dollars)	September 30, 2007	December 31, 2006
Buildings, improvements and construction in progress	$ 2,749,372	$ 2,599,499
Land, including land held for development	536,761	532,871
Total investments in real estate	3,286,133	3,132,370
Accumulated depreciation	(375,013)	(306,893)
Net investments in real estate	$ 2,911,120	$ 2,825,477

Acquisition

In August 2007, the Company purchased a land parcel in Monroe Township, Pennsylvania for $5.5 million. The Company intends to develop this land and other land owned by the Company in the area into a power center to be known as Monroe Marketplace.

Dispositions

In August 2007, the Company sold undeveloped land adjacent to Wiregrass Commons for $2.1 million. The Company recorded a $0.3 million gain on this sale.

In May 2007, the Company sold an outparcel and related land improvements at Plaza at Magnolia for $11.3 million. The Company recorded a $1.5 million gain on the sale.

In May 2007, the Company sold an outparcel and related land improvements containing an operating restaurant at New River Valley Mall for $1.6 million. The Company recorded a $0.6 million gain on the sale.

In March 2007, the Company sold Schuylkill Mall in Frackville, Pennsylvania for $17.6 million. The Company recorded a gain of $6.7 million from this sale. In connection with the sale, the Company repaid the mortgage note associated with Schuylkill Mall, with a balance of $16.5 million at closing.

Discontinued Operations

In accordance with Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS No. 144), the Company has presented as discontinued operations the operating results of Schuylkill Mall, which was sold in March 2007, and South Blanding Village, which was sold in September 2006.

Table of Contents

The following table summarizes revenue and expense information for the Company s discontinued operations:

(in thousands of dollars)	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Real estate revenue	$ 19	$ 1,528	$ 1,056	$ 4,785
Expenses:				
Property operating expenses		(907)	(823)	(2,695)
Interest expense		(300)	(136)	(914)
Depreciation and amortization		(352)	(215)	(3,562)
Total expenses		(1,559)	(1,174)	(7,171)
Operating results from discontinued operations	19	(31)	(118)	(2,386)
Gain on sale of discontinued operations		1,414	6,699	1,414
Minority interest	(1)	(141)	(691)	98
Income (loss) from discontinued operations	$ 18	$ 1,242	$ 5,890	$ (874)

P&S Office Building

During the first quarter of 2007, the Company reclassified P&S Office Building in Gadsden, Alabama for accounting purposes from held for sale to continuing operations. The property no longer meets the conditions for an exception to the one-year classification requirement in SFAS No. 144. The Company intends to continue to actively market P&S Office Building for sale, but at this time, it cannot determine if or when a sale will be consummated. For balance sheet purposes, as of March 31, 2007, the assets and liabilities of P&S Office Building were reclassified from assets held for sale and liabilities related to assets held for sale into the appropriate balance sheet captions. Because P&S Office Building was considered held for sale as of December 31, 2006, no reclassifications related to P&S Office Building were made as of that date. For income statement purposes, the results of operations for the P&S Office Building are presented in continuing operations for all periods presented. In the first quarter of 2007, the Company recorded depreciation and amortization expense of $0.2 million to reflect the depreciation and amortization during all of the period that P&S Office Building was classified as held for sale.

Capitalization of Costs

Costs incurred for interest, real estate taxes and insurance that are directly related to development and redevelopment projects are capitalized only during periods in which activities necessary to prepare the property for its intended use are in progress. Costs incurred for such items after the property is substantially complete and ready for its intended use are charged to expense as incurred. The Company capitalizes a portion of development department employees compensation and benefits related to time spent involved in development and redevelopment projects.

The Company capitalizes payments made to obtain options to acquire real property. All other related costs that are incurred before acquisition of a property are capitalized if the acquisition of the property or if the acquisition of an option to acquire the property is probable. If the property is acquired, such costs are included in the amount recorded as the initial value of the asset. Capitalized pre-acquisition costs are charged to expense when it is no longer probable that the property will be acquired.

The Company capitalizes salaries, commissions and benefits related to time spent by leasing and legal department personnel involved in originating leases with third-party tenants.

The following table summarizes the Company s capitalized salaries and benefits, real estate taxes and interest for the three and nine months ended September 30, 2007 and 2006:

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

(in thousands of dollars)	2007	2006	2007	2006
Development and redevelopment:				
Salaries and benefits	$ 603	$ 723	$ 1,591	$ 1,707
Real estate taxes	$ 520	$ 1,089	$ 1,818	$ 1,328
Interest	$ 4,455	$ 2,799	$ 11,883	$ 6,154
Leasing:				
Salaries and benefits	$ 1,011	$ 1,115	$ 3,502	$ 3,458

Table of Contents

4. INVESTMENTS IN PARTNERSHIPS:

The following table presents summarized financial information of the equity investments in the Company s unconsolidated partnerships as of September 30, 2007 and December 31, 2006:

(in thousands of dollars)	September 30, 2007	December 31, 2006
ASSETS:		
Investments in real estate, at cost:		
Operating properties	$ 345,807	$ 344,909
Construction in progress	34,786	8,312
Total investments in real estate	380,593	353,221
Accumulated depreciation	(84,486)	(75,860)
Net investments in real estate	296,107	277,361
Cash and cash equivalents	634	5,865
Deferred costs and other assets, net	29,807	26,535
Total assets	326,548	309,761
LIABILITIES AND PARTNERS EQUITY/DEFICIT:		
Mortgage notes payable	379,325	382,082
Other liabilities	24,995	18,418
Total liabilities	404,320	400,500
Net deficit	(77,772)	(90,739)