SUN COMMUNITIES INC
Form 10-Q
November 07, 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 September 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 September 30, 2008: 18,411,400

SUN COMMUNITIES, INC.

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SUN COMMUNITIES, INC.

CONSOLIDATED BALANCE SHEETS

AS OF SEPTEMBER 30, 2008 AND DECEMBER 31, 2007

(amounts in thousands, except per share data)

	(Unaudited) September 30, 2008	December 31, 2007
ASSETS		
Investment property, net	$1,108,079	$1,134,204
Cash and cash equivalents	6,824	5,415
Inventory of manufactured homes	10,037	12,082
Investment in affiliates	6,464	20,000
Notes and other receivables	51,074	36,846
Other assets	39,377	37,276
TOTAL ASSETS	$1,221,855	$1,245,823
LIABILITIES		
Debt	$1,141,030	$1,101,972
Lines of credit	71,876	85,703
Other liabilities	37,186	32,102
TOTAL LIABILITIES	1,250,092	1,219,777
Commitments and contingencies	—	—
Minority interest	—	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 (September 30, 2008 and December 31, 2007, 20,213 and 20,228 shares issued respectively)	202	202
Additional paid-in capital	459,598	458,487
Officer's notes	(8,439)	(8,740)
Accumulated other comprehensive loss	(920)	(856)
Distributions in excess of accumulated earnings	(415,078)	(364,446)
Treasury stock, at cost (September 30, 2008 and December 31, 2007, 1,802 shares)	(63,600)	(63,600)
TOTAL STOCKHOLDERS' EQUITY (DEFICIT)	(28,237)	21,047
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)	$1,221,855	$1,245,823

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

SUN COMMUNITIES, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE PERIODS ENDED SEPTEMBER 30, 2008 AND 2007

(amounts in thousands, except for per share data)

(unaudited)

	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
REVENUES				
Income from real property	$47,966	$46,818	$146,365	$142,918
Revenue from home sales	7,933	5,492	24,204	17,847
Rental home revenue	5,186	4,798	15,318	13,933
Ancillary revenues, net	35	4	349	355
Interest	1,129	686	2,741	2,142
Other income (loss)	(816)	(432)	2,884	(526)
Total revenues	61,433	57,366	191,861	176,669
COSTS AND EXPENSES				
Property operating and maintenance	12,766	12,845	37,742	36,698
Real estate taxes	3,844	4,174	12,183	12,369
Cost of home sales	6,073	4,408	18,893	14,164
Rental home operating and maintenance	4,135	3,563	11,566	10,002
General and administrative - real property	3,704	3,709	12,589	11,856
General and administrative - home sales and rentals	1,676	1,462	5,003	4,440
Depreciation and amortization	16,167	15,512	48,527	46,444
Interest	15,361	15,783	45,311	46,164
Interest on mandatorily redeemable debt	847	896	2,535	2,705
Total expenses	64,573	62,352	194,349	184,842
Loss before income taxes, minority interest, and income (loss) from affiliates	(3,140)	(4,986)	(2,488)	(8,173)
Provision for state income tax	(141)	(525)	(34)	(575)
Minority interest in Operating Partnership	(726)	560	602	832
Income (loss) from affiliates	(1,486)	583	(14,036)	1,431
Net loss	$(5,493)	$(4,368)	$(15,956)	$(6,485)
Weighted average common shares outstanding:				
Basic	18,213	17,962	18,151	17,909
Diluted	18,213	17,962	18,151	17,909
Basic and diluted loss per share:	$(0.30)	$(0.24)	$(0.88)	$(0.36)
Cash dividends per common share:	$0.63	$0.63	$1.89	$1.89

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

SUN COMMUNITIES, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

FOR THE PERIODS ENDED SEPTEMBER 30, 2008 AND 2007

(amounts in thousands)

(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	**2007**	**2008**	**2007**
Net loss	$(5,493)	$(4,368)	$(15,956)	$(6,485)
Unrealized gain (loss) on interest rate swaps	4	(1,042)	(64)	(640)
Comprehensive loss	$(5,489)	$(5,410)	$(16,020)	$(7,125)

SUN COMMUNITIES, INC.

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

FOR THE NINE MONTHS ENDED SEPTEMBER 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	—	(458)	—	—	(1)	—	(459)
Stock-based compensation - amortization and forfeitures	—	1,569	—	—	68	—	1,637
Repayment of officer's notes	—	—	301	—	—	—	301
Net loss	—	—	—	—	(15,956)	—	(15,956)

Unrealized loss on interest rate swaps	—	—	—	(64)	—	—	(64)
Cash distributions declared of $1.89 per share	—	—	—	—	(34,743)	—	(34,743)
Balance as of September 30, 2008	$202	$459,598	$(8,439)	$(920)	$(415,078)	$(63,600)	$(28,237)

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

SUN COMMUNITIES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2008 AND 2007

(amounts in thousands)

(unaudited)

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (15,956)	$ (6,485)
Adjustments to reconcile net loss to cash provided by operating activities:		
Net minority interest allocation	(602)	(832)
Gain from land disposition	(3,336)	—
Gain on valuation of derivative instruments	(2)	(250)
Stock compensation expense	1,696	1,798
Depreciation and amortization	50,383	48,935
Amortization of deferred financing costs	1,145	1,066
Distributions from affiliate	—	900
Equity (income) loss from affiliate	14,036	(1,431)
Payments on notes receivable from sale of financed homes	2,848	2,349
Change in inventory, other assets and other receivables, net	(11,718)	(14,785)
Change in accounts payable and other liabilities, net	(1,042)	1,666
Net cash provided by operating activities	37,452	32,931
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investment in properties	(28,232)	(20,179)
Investment in affiliate	(500)	—
Proceeds related to disposition of land	6,508	—
Payments of notes receivable and officer's notes, net	887	13,077
Net cash used for investing activities	(21,337)	(7,102)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Cancellation of common stock and OP units, net	(459)	(1,259)
Proceeds from option exercise	—	38
Payments on lines of credit, net	(13,827)	(10,384)
Payments to retire preferred operating partnership units	—	(4,500)
Proceeds from issuance of notes payable and other debt	52,549	37,500
Payments on notes payable and other debt	(13,538)	(10,916)
Distributions to shareholders and OP unit holders	(39,093)	(34,878)
Payments for deferred financing costs	(338)	(804)
Net cash used for financing activities	(14,706)	(25,203)
Net increase in cash and cash equivalents	1,409	626
Cash and cash equivalents, beginning of period	5,415	3,183
Cash and cash equivalents, end of period	$ 6,824	$ 3,809
SUPPLEMENTAL INFORMATION:		
Cash paid for interest	$ 42,990	$ 44,808
Cash paid for interest on mandatorily redeemable debt	$ 2,587	$ 2,677

Noncash investing and financing activities:		
Unrealized loss on interest rate swaps	$ (64)	$ (640)
Rental homes transferred from inventory	$ 7,027	$ 7,117
Home sales financed by Company	$ 15,958	$ 9,776

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) September 30, 2008	**December 31, 2007**
Land	$ 117,116	$ 117,310
Land improvements and buildings	1,191,298	1,184,257
Rental homes and improvements	179,445	170,227
Furniture, fixtures, and equipment	36,859	36,433
Land held for future development	27,986	30,199
Investment property	1,552,704	1,538,426
Less: Accumulated depreciation	(444,625)	(404,222)
Investment property, net	$ 1,108,079	$ 1,134,204

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

The Company sold approximately 82 acres of undeveloped land that resulted in a $3.3 million gain through the nine months ended September 30, 2008.

3. Secured Borrowing and Collateralized Receivables

During the quarter, the Company completed a transaction involving $25.6 million of its installment loans secured by manufactured homes. The Company received $25.6 million of cash proceeds in exchange for relinquishing its right, title and interest in the installment notes. The Company is subject to certain recourse provisions requiring the Company to purchase the underlying homes collateralizing such notes in the event of a note default and subsequent repossession of the home.

SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

3. Secured Borrowing and Collateralized Receivables, continued

FASB Statement No. 140, “Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities” (“SFAS 140”) sets forth the criteria that must be met for control over transferred assets to be considered to have been surrendered, which includes, amongst other things: (1) the transferred assets have been isolated from the transferor, including put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership, (2) the transferee must obtain the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the transferor cannot maintain effective control over the transferred assets through an agreement to repurchase them before their maturity. When a company transfers financial assets and fails any one of the SFAS 140 criteria, the company is prevented from derecognizing the transferred financial assets and the transaction is accounted for as a secured borrowing. The determination about whether the isolation criteria of SFAS 140 has been met to support a conclusion regarding surrender of control is largely a matter of law. As such, the evidence required for testing whether or not the first criteria of SFAS 140 has been satisfied requires a legal "true sale" opinion analyzing the treatment of the transfer under state laws as if the Company was a debtor under the bankruptcy code. A "true sale" legal opinion includes several legally relevant factors, including the nature of retained interests in the loans sold. Legal opinions as to a "true sale" are never absolute and unconditional, but contain qualifications based on the inherent equitable powers of a bankruptcy court, as well as the unsettled state of the common law.

It was the intent of both parties for the transaction to qualify for sale accounting under SFAS 140 and the terms of the agreement clearly stipulate that the Company has no further obligations or rights with respect to the control, management, administration, servicing, or collection of the installment notes. In addition, the transferee has obtained the right to pledge or exchange the installment loans. For federal tax purposes, the Company treats the transfers of loans which do not qualify as “true sales” under SFAS 140, as sales.

Notwithstanding these facts, the Company was unable to satisfy the first criteria for sale accounting treatment under SFAS 140 and therefore, the Company has recorded the transaction as a transfer of financial assets. The transferred assets have been classified as collateralized receivables and the cash received from this transaction has been classified as a secured borrowing in the consolidated balance sheet.

The collateralized receivables earn interest income and the secured borrowings accrue borrowing costs at the same interest rates. The amount of interest income and expense recognized was $0.7 million for the three and nine months ended September 30, 2008. The collateralized receivables and secured borrowings are reduced as the related installment notes are collected from the customer. The balance of the collateralized receivables was $24.9 million, net of a loan loss provision of $0.1 million as of September 30, 2008. The outstanding balance on the secured borrowing was $25.0 million as of September 30, 2008.

In the event of note default, and subsequent repossession of a manufactured home, the terms of the agreement require the Company to repurchase the manufactured home. Default is defined as the failure to repay the installment note according to contractual terms. If default on the installment note results in repossession of the home, the home is repurchased at a certain percentage of the outstanding principal balance of the installment loan based on the number of payments made on the loan. In general, based on the number of payments made since the loan origination date, the repurchase balance is determined as follows:

Number of Payments	Recourse %	
Less than or equal to 15	100	%
Greater than 15 but less than 64	90	%
64 or more	65	%

SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

4. Notes and Other Receivables

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

Installment loans on manufactured homes with interest payable monthly at a net weighted average interest rate and maturity of 7.2% and 13.1 years and 7.3
Collateralized receivables, net (see Note 3).
Other receivables, net of allowance for losses of $0.3 million at September 30, 2008

and December 31, 2007.
Total notes and other receivables, net

The installment loans of $18.1 million and $30.4 million at September 30, 2008 and December 31, 2007, respectively, are collateralized by manufactured homes. The installment loans are presented net of allowance for losses of $0.1 million and $0.2 million at September 30, 2008 and December 31, 2007, respectively. The loans represent financing provided by the Company to purchasers of manufactured homes located in its communities.

During the quarter, the Company completed a transaction involving approximately $25.6 million of its installment loans. This transaction was accounted for as a transfer of financial assets. The transferred assets have been classified as collateralized receivables. The reduction in the aggregate principal balance of these collateralized receivables was $0.6 million since the transfer occurred. The collateralized receivables of $24.9 million are presented net of allowance for losses of $0.1 million at September 30, 2008. See Note 3 for additional information.

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 September 30, 2008, and December 31, 2007 (in thousands except for shares and units):

	As of September 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	$975	60,007	—	$1,010	62,151	—

Secured - $6.6 million	4,955	133,243	95,857	5,132	138,003	99,282
Secured - $1.0 million	767	70,936	—	794	73,470	—
Unsecured - $1.0 million	767	—	—	794	—	—
Unsecured - $1.3 million	975	—	—	1,010	—	—
Total promissory notes	$ 8,439	264,186	95,857	$ 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 $0.3 million for the nine months ended September 30, 2008 and 2007. Total interest was $0.1 million and $0.2 million for the three months ended September 30, 2008 and 2007, respectively. Total interest was $0.4 million and $0.5 million for the nine months ended September 30, 2008 and 2007, respectively.

SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

5. Investment in Affiliates

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 September 30, 2008, and its investment is accounted for using the equity method of accounting.

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. In the ensuing months, Origen followed its Asset Disposition and Management Plan and Origen sold $176 million of unsecuritized loans, its servicing platform, and its origination platform. 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.

Equity loss from affiliate recorded for the three months ended September 30, 2008, reflects the Company’s estimate of its portion of the anticipated loss from Origen of $0.2 million, as well as an other than temporary impairment loss of $1.3 million. Equity loss from affiliate recorded for the nine months ended September 30, 2008, reflects the Company’s estimate of its portion of the anticipated loss from Origen of $6.0 million, as well as an other than temporary impairment loss of $8.1 million.

6. Debt and Lines of Credit

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

	September 30, 2008	**December 31, 2007**
Collateralized term loans - CMBS, 4.93-5.32%, due July 1, 2011-2016.	$480,765	$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 3.75 - 5.20% at September 30, 2008 and 4.51 - 5.20% at December 31, 2007.	378,663	381,587
Preferred OP units, redeemable at various dates from December 1, 2009 through January 2, 2014, average interest at 6.8% at September 30, 2008, and 7.2% at December 31, 2007.	49,447	49,447
Secured borrowing, maturing at various dates from May 5, 2009 through May 16, 2028, average interest at 10.0% at September 30, 2008 (see Note 3).	25,023	—
Mortgage notes, other, maturing at various dates from June 1, 2009 through May 1, 2017, average interest at 5.72% at September 30, 2008 and 6.10% at December 31, 2007.	207,132	184,875

Total debt	$ 1,141,030	$ 1,101,972

The collateralized term loans totaling $859.4 million at September 30, 2008, are secured by 87 properties comprising of 31,143 sites representing approximately $564.8 million of net book value. The mortgage notes totaling $207.1 million at September 30, 2008, are collateralized by 18 communities comprising of 6,423 sites representing approximately $182.7 million of net book value.

SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

6. Debt and Lines of Credit, continued

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 September 30, 2008 and December 31, 2007, was $64.3 million and $85.4 million, respectively. In addition, $3.4 million of availability was used to back standby letters of credit at September 30, 2008 and December 31, 2007. Borrowings under the line of credit bear an interest rate of LIBOR plus 165 basis points, or Prime plus 40 basis points. The Company has the option to borrow at either rate, and will select the rate that results in a lower borrowing cost. The borrowings under the line of credit mature October 1, 2011 with the election of a one year extension that is available at the Company's discretion. At September 30, 2008 and December 31, 2007, $47.3 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.

The Company also has the potential to utilize a floor plan facility that allows for draws on new home purchases up to $40.0 million. At September 30, 2008 and December 31, 2007, the outstanding balance on the floor plan was $7.6 million and $0.3 million, respectively. The facility matures on March 1, 2009, and bears interest at Prime (5.00% at September 30, 2008). Prime means for any month, the prevailing "prime rate" as quoted in the Wall Street Journal on last day of such calendar month.

The Company completed a financing of $27.0 million with a bank in June 2008. 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, (5.25% at September 30, 2008). 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.

During the quarter, the Company completed a transaction involving $25.6 million of its installment loans. This transaction was accounted for as a transfer of financial assets and the cash proceeds related to this transaction were recorded as a secured borrowing. See Note 3 for additional information.

At September 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					
		Oct 2008-	**Oct 2009 -**	**Oct 2010 -**	**Oct 2011 -**	**Oct 2012 -**	**After**
	Total Due	**Sept 2009**	**Sept 2010**	**Sept 2011**	**Sept 2012**	**Sept 2013**	**5 years**
Debt	$1,116,007	$23,483	$22,099	$121,941	$26,733	$38,511	$883,240
Secured borrowing	25,023	1,019	1,125	1,228	1,349	1,433	18,869
Lines of credit	71,876	7,576	—	—	64,300	—	—
Total	$1,212,906	$32,078	$23,224	$123,169	$92,382	$39,944	$902,109

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 September 30, 2008, and December 31, 2007, the Company was in compliance with all covenants.

7. Share-Based Compensation

The Company’s primary share-based 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.

SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

7. Share-Based Compensation, continued

On July 10, 2008, the Company executed 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 communicated and accepted by Mr. Fannon prior to the end of the second quarter, the compensation expense was recorded in that period.

In July 2008, the Company issued 10,500 director options under its 2004 Non-Employee Director Option Plan. The weighted average fair value of the options issued is estimated on the date of the grant using the Binomial (lattice) option pricing model, with the following weighted average assumptions used for the grants in the period indicated:

	July 2008 Award	
Estimated fair value per share of options granted:	$ 1.17	
Assumptions:		
Annualized dividend yield	14.70	%
Common stock price volatility	22.14	%
Risk-free rate of return	3.63	%
Expected option terms (in years)	7.3	

8. Other Income

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Brokerage commissions	$ 114	$ 168	$ 474	$ 541
Gain on sale of undeveloped land	33	—	3,336	—
Loss on disposition of assets, net	(615)	(724)	(528)	(1,193)
Other	(348)	124	(398)	126

Total other income (loss)	$ (816)	$ (432)	$ 2,884	$ (526)

SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

9. Segment Reporting

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

	Three months ended September 30, 2008			Nine months ended September 30, 2008		
	Real Property Operations	Home Sales and Home Rentals	Consolidated	Real Property Operations	Home Sales and Home Rentals	Consolidated
Revenues	$ 47,966 (2)	$ 13,119	$ 61,085	$ 146,365 (2)	$ 39,522	$ 185,887
Operating expenses/Cost of sales	16,610	10,208	26,818	49,925	30,459	80,384
Net operating income[(1)]/Gross profit	31,356	2,911	34,267	96,440	9,063	105,503
Adjustments to arrive at net loss:						
Other revenues	317	31	348	4,924	1,050	5,974
General and administrative	(3,704)	(1,676)	(5,380)	(12,589)	(5,003)	(17,592)
Depreciation and amortization	(11,456)	(4,711)	(16,167)	(34,603)	(13,924)	(48,527)
Interest expense	(16,103)	(105)	(16,208)	(47,618)	(228)	(47,846)
Equity income (loss) from affiliate	(1,500)	14	(1,486)	(14,050)	14	(14,036)
Provision for state income taxes	(141)	—	(141)	(34)	—	(34)
Minority interest	(726)	—	(726)	602	—	602
Net loss	$ (1,957)	$ (3,536)	$ (5,493)	$ (6,928)	$ (9,028)	$ (15,956)

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SUN COMMUNITIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

9. Segment Reporting (amounts in thousands), continued

	Three months ended September 30, 2007			Nine months ended September 30, 2007		
	Real Property Operations	Home Sales and Home Rentals	Consolidated	Real Property Operations	Home Sales and Home Rentals	Consolidated
Revenues	$46,818 (2)	$10,290	$57,108	$142,918 (2)	$ 31,780	$ 174,698
Operating expenses/Cost of sales	17,019	7,971	24,990	49,067	24,166	73,233
Net operating income[1]/Gross profit	29,799	2,319	32,118	93,851	7,614	101,465
Adjustments to arrive at net loss:						
Other revenues (expenses)	281	(23)	258	1,683	288	1,971
General and administrative	(3,709)	(1,462)	(5,171)	(11,856)	(4,440)	(16,296)
Depreciation and amortization	(11,281)	(4,231)	(15,512)	(34,093)	(12,351)	