FEDERAL REALTY INVESTMENT TRUST
Form 10-Q
May 01, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

ý QUARTERLY REPORT PURSUANT TO THE SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2013
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: 1-07533
FEDERAL REALTY INVESTMENT TRUST
(Exact Name of Registrant as Specified in its Declaration of Trust)

Maryland	52-0782497
(State of Organization)	(IRS Employer Identification No.)
1626 East Jefferson Street, Rockville, Maryland	20852
(Address of Principal Executive Offices)	(Zip Code)

(301) 998-8100
(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. ý Yes ¨ No

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ý Yes ¨ 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 definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer	ý	Accelerated Filer	¨
Non-Accelerated Filer	o (Do not check if a smaller reporting company)	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 ý No

The number of Registrant’s common shares outstanding on April 26, 2013 was 65,243,839.

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FEDERAL REALTY INVESTMENT TRUST
QUARTERLY REPORT ON FORM 10-Q
QUARTER ENDED MARCH 31, 2013

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PART I—FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

The following balance sheet as of December 31, 2012, which has been derived from audited financial statements, and unaudited interim financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles (GAAP) have been omitted pursuant to those rules and regulations, although the company believes that the disclosures made are adequate to make the information not misleading. It is suggested that these financial statements be read in conjunction with the financial statements and notes thereto included in the company's latest Annual Report on Form 10-K. In the opinion of management, all adjustments (consisting of normal, recurring adjustments) necessary for a fair presentation for the periods presented have been included. The results of operations for the three months ended March 31, 2013 are not necessarily indicative of the results that may be expected for the full year.

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Federal Realty Investment Trust
Consolidated Balance Sheets

	March 31, 2013	December 31, 2012
	(In thousands, except share data)	
	(Unaudited)	
ASSETS		
Real estate, at cost		
Operating (including $278,885 and $278,826 of consolidated variable interest entities, respectively)	$ 4,497,312	$ 4,490,960
Construction-in-progress	327,840	288,714
	4,825,152	4,779,674
Less accumulated depreciation and amortization (including $13,801 and $12,024 of consolidated variable interest entities, respectively)	(1,257,767)	(1,224,295)
Net real estate	3,567,385	3,555,379
Cash and cash equivalents	31,274	36,988
Accounts and notes receivable, net	77,154	73,861
Mortgage notes receivable, net	55,693	55,648
Investment in real estate partnership	33,131	33,169
Prepaid expenses and other assets	131,192	132,659
Debt issuance costs, net of accumulated amortization of $10,881 and $10,140, respectively	10,103	10,861
TOTAL ASSETS	$ 3,905,932	$ 3,898,565
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Mortgages payable (including $204,681 and $205,299 of consolidated variable interest entities, respectively)	$ 747,978	$ 760,789
Capital lease obligations	71,687	71,693
Notes payable	299,595	299,575
Senior notes and debentures	1,076,635	1,076,545
Accounts payable and accrued expenses	126,715	120,929
Dividends payable	47,977	47,685
Security deposits payable	13,065	12,957
Other liabilities and deferred credits	94,501	103,379
Total liabilities	2,478,153	2,493,552
Commitments and contingencies (Note 6)		
Redeemable noncontrolling interests	94,249	94,420
Shareholders' equity		
Preferred shares, authorized 15,000,000 shares, $.01 par: 5.417% Series 1 Cumulative Convertible Preferred Shares, (stated at liquidation preference $25 per share), 399,896 shares issued and outstanding	9,997	9,997
Common shares of beneficial interest, $.01 par, 100,000,000 shares authorized, 65,239,183 and 64,815,446 shares issued and outstanding, respectively	653	648
Additional paid-in capital	1,910,200	1,875,525
Accumulated dividends in excess of net income	(600,024)	(586,970)
Accumulated other comprehensive loss	(10,773)	(12,388)
Total shareholders' equity of the Trust	1,310,053	1,286,812
Noncontrolling interests	23,477	23,781

Total shareholders’ equity	1,333,530	1,310,593
TOTAL LIABILITIES AND SHAREHOLDERS’ EQUITY	$ 3,905,932	$ 3,898,565

The accompanying notes are an integral part of these consolidated statements.

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Federal Realty Investment Trust
Consolidated Statements of Comprehensive Income
(Unaudited)

	Three Months Ended March 31,	
	2013	2012
	(In thousands, except per share data)	
REVENUE		
Rental income	$ 153,219	$ 140,661
Other property income	3,268	4,362
Mortgage interest income	1,265	1,266
Total revenue	157,752	146,289
EXPENSES		
Rental expenses	29,515	26,110
Real estate taxes	17,651	16,057
General and administrative	7,057	7,004
Depreciation and amortization	40,624	36,571
Total operating expenses	94,847	85,742
OPERATING INCOME	62,905	60,547
Other interest income	30	207
Interest expense	(27,405)	(28,793)
Income from real estate partnerships	312	301
INCOME FROM CONTINUING OPERATIONS	35,842	32,262
Gain on sale of real estate in real estate partnership	—	11,860
NET INCOME	35,842	44,122
Net income attributable to noncontrolling interests	(1,254)	(1,136)
NET INCOME ATTRIBUTABLE TO THE TRUST	34,588	42,986
Dividends on preferred shares	(135)	(135)
NET INCOME AVAILABLE FOR COMMON SHAREHOLDERS	$ 34,453	$ 42,851
EARNINGS PER COMMON SHARE, BASIC		
Continuing operations	$ 0.53	$ 0.48
Gain on sale of real estate	—	0.19
	$ 0.53	$ 0.67
Weighted average number of common shares, basic	64,692	63,411
EARNINGS PER COMMON SHARE, DILUTED		
Continuing operations	$ 0.53	$ 0.48
Gain on sale of real estate	—	0.19
	$ 0.53	$ 0.67
Weighted average number of common shares, diluted	64,847	63,585
COMPREHENSIVE INCOME	$ 37,457	$ 45,480
COMPREHENSIVE INCOME ATTRIBUTABLE TO THE TRUST	$ 36,203	$ 44,344

The accompanying notes are an integral part of these consolidated statements.

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Federal Realty Investment Trust
Consolidated Statement of Shareholders' Equity
For the Three Months Ended March 31, 2013
(Unaudited)

	Shareholders' Equity of the Trust								
	Preferred Shares		Common Shares						
	Shares	Amount	Shares	Amount	Additional Paid-in Capital	Accumulated Dividends in Excess of Net Income	Accumulated Other Comprehensive Loss	Noncontrolling Interests	Total Shareholders' Equity
	(In thousands, except share data)								
BALANCE AT DECEMBER 31, 2012	399,896	$9,997	64,815,446	$648	$1,875,525	$(586,970)	$(12,388)	$23,781	$1,310,593
Net income, excluding $723 attributable to redeemable noncontrolling interests	—	—	—	—	—	34,588	—	531	35,119
Other comprehensive income - change in value of interest rate swaps	—	—	—	—	—	—	1,615	—	1,615
Dividends declared to common shareholders	—	—	—	—	—	(47,507)	—	—	(47,507)
Dividends declared to preferred shareholders	—	—	—	—	—	(135)	—	—	(135)
Distributions declared to noncontrolling interests	—	—	—	—	—	—	—	(385)	(385)
Common shares issued	—	—	302,087	4	32,190	—	—	—	32,194
Exercise of stock options	—	—	6,125	—	239	—	—	—	239
Shares issued under dividend reinvestment plan	—	—	5,293	—	559	—	—	—	559
Share-based compensation expense, net of shares withheld for employee	—	—	87,756	1	1,237	—	—	—	1,238

taxes									
Conversion and redemption of OP units	—	—	22,476	—	450	—	—	(450)	—
BALANCE AT MARCH 31, 2013	399,896	$9,997	65,239,183	$653	$1,910,200	$(600,024)	$(10,773)	$23,477	$1,333,530

The accompanying notes are an integral part of these consolidated statements.

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Federal Realty Investment Trust
Consolidated Statements of Cash Flows
(Unaudited)

	Three Months Ended March 31,	
	2013	2012
	(In thousands)	
OPERATING ACTIVITIES		
Net income	$35,842	$44,122
Adjustment to reconcile net income to net cash provided by operating activities		
Depreciation and amortization, including discontinued operations	40,624	36,571
Gain on sale of real estate in real estate partnership	—	(11,860)
Income from real estate partnerships	(312)	(301)
Other, net	(61)	2,121
Changes in assets and liabilities, net of effects of acquisitions and dispositions:		
(Increase) decrease in accounts receivable	(2,458)	740
Increase in prepaid expenses and other assets	(93)	(398)
Increase (decrease) in accounts payable and accrued expenses	1,435	(1,734)
(Decrease) increase in security deposits and other liabilities	(7,284)	196
Net cash provided by operating activities	67,693	69,457
INVESTING ACTIVITIES		
Capital expenditures - development and redevelopment	(33,367)	(24,081)
Capital expenditures - other	(9,460)	(12,958)
Distribution from real estate partnership in excess of earnings	—	143
Leasing costs	(2,723)	(2,243)
Issuance of mortgage and other notes receivable, net	(125)	(143)
Net cash used in investing activities	(45,675)	(39,282)
FINANCING ACTIVITIES		
Repayment of mortgages, capital leases and notes payable	(12,095)	(3,292)
Issuance of common shares	32,542	22,402
Dividends paid to common and preferred shareholders	(46,884)	(43,497)
Distributions to and redemptions of noncontrolling interests	(1,295)	(4,412)
Net cash used in financing activities	(27,732)	(28,799)
(Decrease) increase in cash and cash equivalents	(5,714)	1,376
Cash and cash equivalents at beginning of year	36,988	67,806
Cash and cash equivalents at end of period	$31,274	$69,182

The accompanying notes are an integral part of these consolidated statements.

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Federal Realty Investment Trust
Notes to Consolidated Financial Statements
March 31, 2013
(Unaudited)

NOTE 1—BUSINESS AND ORGANIZATION

Federal Realty Investment Trust (the “Trust”) is an equity real estate investment trust (“REIT”) specializing in the ownership, management, and redevelopment of retail and mixed-use properties. Our properties are located primarily in densely populated and affluent communities in strategically selected metropolitan markets in the Mid-Atlantic and Northeast regions of the United States, and California. As of March 31, 2013, we owned or had a majority interest in community and neighborhood shopping centers and mixed-use properties which are operated as 88 predominantly retail real estate projects.

We operate in a manner intended to enable us to qualify as a REIT for federal income tax purposes. A REIT that distributes at least 90% of its taxable income to its shareholders each year and meets certain other conditions is not taxed on that portion of its taxable income which is distributed to its shareholders. Therefore, federal income taxes on our taxable income have been and are generally expected to be immaterial. We are obligated to pay state taxes, generally consisting of franchise or gross receipts taxes in certain states. Such state taxes also have not been material.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

Our consolidated financial statements include the accounts of the Trust, its corporate subsidiaries, and all entities in which the Trust has a controlling interest or has been determined to be the primary beneficiary of a variable interest entity (“VIE”). The equity interests of other investors are reflected as noncontrolling interests or redeemable noncontrolling interests. All significant intercompany transactions and balances are eliminated in consolidation. We account for our interests in joint ventures, which we do not control, using the equity method of accounting. Certain 2012 amounts have been reclassified to conform to current period presentation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America, referred to as “GAAP,” requires management to make estimates and assumptions that in certain circumstances affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and revenues and expenses. These estimates are prepared using management’s best judgment, after considering past, current and expected events and economic conditions. Actual results could differ from these estimates.

Recently Adopted Accounting Pronouncements

In February 2013, the FASB issued ASU 2013-2, “Comprehensive Income (Topic 220): Reporting Amounts Reclassified Out of Accumulated Other Comprehensive Income.” ASU 2013-2 requires entities to disclose certain information relating to amounts reclassified out of accumulated other comprehensive income. We adopted the standard effective January 1, 2013 and it did not have a significant impact to our consolidated financial statements.

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Consolidated Statements of Cash Flows—Supplemental Disclosures

The following table provides supplemental disclosures related to the Consolidated Statements of Cash Flows:

	Three Months Ended March 31,	
	2013	2012
	(In thousands)	
SUPPLEMENTAL DISCLOSURES:		
Total interest costs incurred	$30,241	$31,250
Interest capitalized	(2,836)	(2,457)
Interest expense	$27,405	$28,793
Cash paid for interest, net of amounts capitalized	$30,315	$31,669
Cash paid for income taxes	$294	$177
NON-CASH FINANCING TRANSACTION:		
Shares issued under dividend reinvestment plan	$(450)	$(487)

NOTE 3—REAL ESTATE PARTNERSHIP

We have a joint venture arrangement (the “Partnership”) with affiliates of a discretionary fund created and advised by ING Clarion Partners (“Clarion”). We own 30% of the equity in the Partnership and Clarion owns 70%. We hold a general partnership interest, however, Clarion also holds a general partnership interest and has substantive participating rights. We cannot make significant decisions without Clarion’s approval. Accordingly, we account for our interest in the Partnership using the equity method. As of March 31, 2013, the Partnership owned seven retail real estate properties. We are the manager of the Partnership and its properties, earning fees for acquisitions, dispositions, management, leasing, and financing. Intercompany profit generated from fees is eliminated in consolidation. We also have the opportunity to receive performance-based earnings through our Partnership interest. Accounting policies for the Partnership are similar to accounting policies followed by the Trust. The Partnership is subject to a buy-sell provision which is customary for real estate joint venture agreements and the industry. Either partner may initiate this provision at any time, which could result in either the sale of our interest or the use of available cash or borrowings to acquire Clarion’s interest.

The following tables provide summarized operating results and the financial position of the Partnership:

	Three Months Ended March 31,	
	2013	2012
	(In thousands)	
OPERATING RESULTS		
Revenue	$4,949	$4,589
Expenses		
Other operating expenses	1,817	1,339
Depreciation and amortization	1,369	1,376
Interest expense	842	845
Total expenses	4,028	3,560
Net income	$921	$1,029
Our share of net income from real estate partnership	$312	$358

	March 31, 2013	December 31, 2012
	(In thousands)	
BALANCE SHEETS		
Real estate, net	$173,356	$174,509
Cash	3,745	2,735
Other assets	4,924	5,536
Total assets	$182,025	$182,780
Mortgages payable	$57,098	$57,155
Other liabilities	3,914	4,771
Partners' capital	121,013	120,854
Total liabilities and partners' capital	$182,025	$182,780
Our share of unconsolidated debt	$17,130	$17,147
Our investment in real estate partnership	$33,131	$33,169

NOTE 4—DEBT

On January 2, 2013, we repaid the mortgage loan on White Marsh Plaza prior to its original maturity date at par for $9.0 million. The loan had an original maturity date of April 1, 2013.

During the three months ended March 31, 2013, the maximum amount of borrowing outstanding under our $400.0 million revolving credit facility was $36.0 million. The weighted average borrowings outstanding was $16.9 million, and the weighted average interest rate before amortization of debt fees was 1.37%. At March 31, 2013, there was no balance outstanding. Our revolving credit facility, term loan and certain notes require us to comply with various financial covenants, including the maintenance of minimum shareholders' equity and debt coverage ratios and a maximum ratio of debt to net worth. As of March 31, 2013, we were in compliance with all loan covenants.

NOTE 5—FAIR VALUE OF FINANCIAL INSTRUMENTS

Except as disclosed below, the carrying amount of our financial instruments approximates their fair value. The fair value of our mortgages payable, notes payable and senior notes and debentures is sensitive to fluctuations in interest rates. Quoted market prices (Level 1) were used to estimate the fair value of our marketable senior notes and debentures and discounted cash flow analysis (Level 2) is generally used to estimate the fair value of our mortgages and notes payable. Considerable judgment is necessary to estimate the fair value of financial instruments. The estimates of fair value presented herein are not necessarily indicative of the amounts that could be realized upon disposition of the financial instruments. A summary of the carrying amount and fair value of our mortgages payable, notes payable and senior notes and debentures is as follows:

	March 31, 2013		December 31, 2012	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(In thousands)			
Mortgages and notes payable	$1,047,573	$1,093,060	$1,060,364	$1,110,757
Senior notes and debentures	$1,076,635	$1,190,833	$1,076,545	$1,190,833

As of March 31, 2013, we have two interest rate swap agreements with a notional amount of $275.0 million that are measured at fair value on a recurring basis. The interest rate swap agreements fix the variable portion of our $275.0 million term loan at 1.72% from December 1, 2011 through November 1, 2018, and effectively fix the rate of the term loan at 3.17%. We assess effectiveness of our cash flow hedges both at inception and on an ongoing basis. The effective portion of changes in fair value of the interest rate swaps associated with our cash flow hedges is recorded in accumulated other comprehensive income/loss and is subsequently reclassified into interest expense as interest is incurred on the related variable rate debt. Within the next 12 months, we expect to reclassify an estimated $4.1 million as an increase to interest expense. Our cash flow hedges become ineffective if critical terms of the hedging instrument and the debt instrument do not perfectly match such as notional amounts, settlement dates, reset dates, calculation period and LIBOR rate. In addition, we evaluate the default risk of the counterparty by monitoring the credit-worthiness of the counterparty. When ineffectiveness exists, the ineffective portion of changes in fair value of the interest rate swaps associated with our cash flow hedges is recognized in earnings in the period affected. Hedge ineffectiveness has not impacted earnings as of March 31, 2013, and we do not anticipate it will have a significant effect in the future.

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The fair values of the interest rate swap agreements are based on the estimated amounts we would receive or pay to terminate the contracts at the reporting date and are determined using interest rate pricing models and interest rate related observable inputs. The fair value of our swaps at March 31, 2013 was a liability of $10.8 million and is included in "accounts payable and accrued expenses" on our consolidated balance sheet. The change in valuation on our interest rate swaps was $1.6 million (including $1.0 million reclassified from other comprehensive loss to interest expense) for the three months ended March 31, 2013 and is included in "accumulated other comprehensive loss".
A summary of our financial liabilities that are measured at fair value on a recurring basis, by level within the fair value hierarchy is as follows:

	March 31, 2013				December 31, 2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
	(In thousands)							
Interest rate swaps	$—	$10,773	$—	$10,773	$—	$12,388	$—	$12,388

NOTE 6—COMMITMENTS AND CONTINGENCIES
We are sometimes involved in lawsuits, warranty claims, and environmental matters arising in the ordinary course of business. Management makes assumptions and estimates concerning the likelihood and amount of any potential loss relating to these matters.
We are currently a party to various legal proceedings. We accrue a liability for litigation if an unfavorable outcome is probable and the amount of loss can be reasonably estimated. If an unfavorable outcome is probable and a reasonable estimate of the loss is a range, we accrue the best estimate within the range; however, if no amount within the range is a better estimate than any other amount, the minimum within the range is accrued. Legal fees related to litigation are expensed as incurred. We do not believe that the ultimate outcome of these matters, either individually or in the aggregate, could have a material adverse effect on our financial position or overall trends in results of operations; however, litigation is subject to inherent uncertainties. Also under our leases, tenants are typically obligated to indemnify us from and against all liabilities, costs and expenses imposed upon or asserted against us (1) as owner of the properties due to certain matters relating to the operation of the properties by the tenant, and (2) where appropriate, due to certain matters relating to the ownership of the properties prior to their acquisition by us.
Under the terms of certain partnership agreements, the partners have the right to exchange their operating partnership units for cash or the same number of our common shares, at our option. A total of 298,170 operating partnership units are outstanding which have a total fair value of $32.2 million, based on our closing stock price on March 31, 2013.

NOTE 7—SHAREHOLDERS' EQUITY
The following table provides a summary of dividends declared and paid per share:

	Three Months Ended March 31,			
	2013		2012	
	Declared	Paid	Declared	Paid
Common shares	$0.730	$0.730	$0.690	$0.690
5.417% Series 1 Cumulative Convertible Preferred shares	$0.339	$0.339	$0.339	$0.339

We have an at the market ("ATM") equity program in which we may from time to time offer and sell common shares having an aggregate offering price of up to $300.0 million. We intend to use the net proceeds to fund potential acquisition opportunities, fund our development and redevelopment pipeline, repay amounts outstanding under our revolving credit facility and/or for general corporate purposes. For the three