SALESFORCE COM INC
Form 4
July 01, 2015

FORM 4

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. *See* Instruction 1(b).

STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

OMB APPROVAL

OMB Number:	3235-0287
Expires:	January 31, 2005
Estimated average burden hours per response...	0.5

(Print or Type Responses)

1. Name and Address of Reporting Person *
Martinez Maria

(Last) (First) (Middle)

THE LANDMARK @ ONE MARKET ST, SUITE 300

(Street)

SAN FRANCISCO, CA 94105

(City) (State) (Zip)

2. Issuer Name **and** Ticker or Trading Symbol
SALESFORCE COM INC [CRM]

3. Date of Earliest Transaction (Month/Day/Year)
06/30/2015

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

_____ Director _____ 10% Owner
__X__ Officer (give title below) _____ Other (specify below)
Pres., Sales & Cust. Success

6. Individual or Joint/Group Filing(Check Applicable Line)
_X_ Form filed by One Reporting Person
___ Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1.Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Common Stock	06/30/2015 (1)		M		5,792	A	$ 27.0625	41,333	D	
Common Stock	06/30/2015 (1)		S		4,189	D	$ 69.8779 (2)	37,144	D	
Common Stock	06/30/2015 (1)		S		1,603	D	$ 70.4921 (3)	35,541	D	
Common Stock	06/30/2015 (1)		M		3,505	A	$ 35.865	39,046	D	
	06/30/2015 (1)		S		2,755	D		36,291	D	

Common Stock							$ 69.968 (4)			
Common Stock	06/30/2015 (1)		S		750	D	$ 70.524 (5)	35,541	D	
Common Stock	06/30/2015 (1)		S		2,202	D	$ 69.8986 (6)	33,339	D	
Common Stock	06/30/2015 (1)		S		700	D	$ 70.4914 (7)	32,639	D	

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474 (9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned
(*e.g.*, puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)		5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)		6. Date Exercisable and Expiration Date (Month/Day/Year)		7. Title and Amo Underlying Secu (Instr. 3 and 4)	
				Code	V	(A)	(D)	Date Exercisable	Expiration Date	Title	Am or Nu of Sh
Non-qualified Stock Option (Right to Buy)	$ 27.0625	06/30/2015 (1)		M			5,792	11/22/2012 (8)	11/22/2016	Common Stock	5
Non-qualified Stock Option (Right to Buy)	$ 35.865	06/30/2015 (1)		M			3,505	02/28/2013 (9)	02/28/2017	Common Stock	3

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
Martinez Maria THE LANDMARK @ ONE MARKET ST SUITE 300			Pres., Sales & Cust. Success	

SAN FRANCISCO, CA 94105

Signatures

/s/ Scott Siamas, attorney-in-fact for Maria Martinez | 07/01/2015

**Signature of Reporting Person | Date

Explanation of Responses:

* If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).

** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

(1) Pursuant to a 10b5-1 Plan.

(2) Weighted average price. These shares were sold in multiple transactions at prices ranging from $69.40 to $70.40 inclusive. The reporting person undertakes to provide to the issuer, any security holder of the issuer, or the staff of the Securities and Exchange Commission, upon request, full information regarding the number of shares sold at each separate price within the range set forth above.

(3) Weighted average price. These shares were sold in multiple transactions at prices ranging from $70.42 to $70.68 inclusive. The reporting person undertakes to provide to the issuer, any security holder of the issuer, or the staff of the Securities and Exchange Commission, upon request, full information regarding the number of shares sold at each separate price within the range set forth above.

(4) Weighted average price. These shares were sold in multiple transactions at prices ranging from $69.47 to $70.44 inclusive. The reporting person undertakes to provide to the issuer, any security holder of the issuer, or the staff of the Securities and Exchange Commission, upon request, full information regarding the number of shares sold at each separate price within the range set forth above.

(5) Weighted average price. These shares were sold in multiple transactions at prices ranging from $70.49 to $70.68 inclusive. The reporting person undertakes to provide to the issuer, any security holder of the issuer, or the staff of the Securities and Exchange Commission, upon request, full information regarding the number of shares sold at each separate price within the range set forth above.

(6) Weighted average price. These shares were sold in multiple transactions at prices ranging from $69.42 to $70.42 inclusive. The reporting person undertakes to provide to the issuer, any security holder of the issuer, or the staff of the Securities and Exchange Commission, upon request, full information regarding the number of shares sold at each separate price within the range set forth above.

(7) Weighted average price. These shares were sold in multiple transactions at prices ranging from $70.44 to $70.53 inclusive. The reporting person undertakes to provide to the issuer, any security holder of the issuer, or the staff of the Securities and Exchange Commission, upon request, full information regarding the number of shares sold at each separate price within the range set forth above.

(8) Option is exercisable and vests over four years at the rate of 25% on November 22, 2012, the first anniversary of the holder's date of grant, with the balance vesting in equal monthly installments over the remaining 36 months.

(9) Option is exercisable and vests over four years at the rate of 25% on February 28, 2013, the first anniversary of the holder's date of grant, with the balance vesting in equal monthly installments over the remaining 36 months.

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *see* Instruction 6 for procedure.
Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. er the stock repurchase program. As of September 30, 2003, the weighted average rate of interest on mortgage debt is 6.40% and the weighted average maturity is approximately 8 years. Approximately 93% of the debt is fixed rate. This limits the exposure to changes in interest rates, minimizing the effect on results of operations and financial condition. Off-Balance Sheet Investments The Company has investments in and advances to approximately 93 affordable housing limited partnerships where the Company acts as the managing general partner. The Company accounts for these investments on the equity method of accounting, recording its share of the net income or loss based upon the terms of the partnership agreement. To the extent that it is determined that the limited partners cannot absorb their share of the losses, if any, the general partner will record the limited partners' share of such losses. The Company guaranteed the low income housing tax credits to the limited partners for a period of five years (from the date of property development under the tax credit program) in 75 partnerships totaling approximately $63.8 million. Such guarantee requires the Company to operate the properties in compliance with Internal Revenue Code Section 42 for 15 years. The weighted average number of compliance years remaining is approximately 10 years. In addition, acting as the general partner in certain partnerships, the Company is obligated to advance funds to meet partnership operating deficits. However, such funding requirements cease after a five-year period. If operating deficits continue to occur after the expiration of the five-year period, the Company would determine on an individual

partnership basis if it is in the best interest of the Company to continue to fund these deficits. The Company believes the properties' operations conform to the applicable requirements as set forth above and do not anticipate any payment on the tax credit guarantees described above. These partnerships are funded with non-recourse financing. The Company's proportionate share of non-recourse financing was $2.6 million at September 30, 2003. The Company has guaranteed a total of $596 of debt associated with two of these partnerships. In addition, the Company, including the Management Companies, has provided loans and advances to certain of the partnerships aggregating $6.3 million at September 30, 2003. The Company assesses the financial status and cash flow of each of the partnerships at each balance sheet date in order to assess recoverability of its investment in and advances to these affiliates. In December 2002, the Company, including its equity affiliates, determined that it would market for sale virtually all of the assets associated with its interest in the aforementioned affordable housing limited partnerships. Such assets include the equity interest in the affordable housing partnerships, loans, advances and management contracts. The Company intends to sell the assets in three phases: Phase I consisting of the Company's interest in 35 properties containing 1,119 units, of which all were New York State Rural Development properties, was sold on September 5, 2003. The sale price of $1,540 resulted in a gain on sale of approximately $72 that was recorded in the third quarter. Not included in the above closing but part of the Phase I contract is one property with 24 units expected to close in the first quarter of 2004. Phase II consists of the Company's interest in 51 properties with 1,519 units, all Pennsylvania, New York and Ohio Rural Development properties. An offer has been accepted for approximately book value and the final contract has been negotiated. The Company anticipates closing on this phase during the fourth quarter of 2003. Phase III consists of the Company's interest in the remaining 37 properties with 3,583 units, primarily located in Upstate New York, Ohio and Maryland. The Company has received competitive bids and has selected a qualified buyer and is working towards a closing anticipated in the first quarter of 2004. The Company has one property with 24 units in Rochester, New York under contract and is expected to close in the fourth quarter of 2003. In addition, the Company has two partnerships in Pittsburgh, Pennsylvania with 1,072 units that are being marketed for sale separately. The Company plans on retaining the general partner interest in one 77-unit property located in Rochester, New York. The property is 80% market rate and is managed as a market rate community. The Company recorded impairment charges aggregating $3,099 during the first nine months of 2003. Of this balance, $1,403 relates to monies loaned to certain equity affiliates to fund operating shortfalls, which are not anticipated to be recovered from projected sale proceeds. The remaining $1,696 pertains to an additional net impairment charge taken on Phase III to reduce the assets to fair market value. The Company's ability to sell the affordable assets on the timelines described above is dependent on a variety of factors, some of which are outside of the Company's control, such as the receipt of the approvals of various partners, lenders and governmental agencies necessary for the sale. Acquisitions and Dispositions In connection with the acquisition of an apartment community, the Company performs a valuation and allocation to each asset and liability acquired in such transaction, based on their estimated fair values at the date of acquisition in accordance with SFAS No. 141 "Business Combinations." The valuation of assets acquired includes both tangible and intangible assets. Tangible asset values, consisting of land, buildings and appliances, are reflected in real estate assets and depreciated over their estimated useful lives. Intangible asset values, consisting of above/below market in place leases, leasehold interest costs, and resident relationships, are reflected in other assets and other liabilities and amortized over the weighted average remaining lease term for in place leases and leasehold interest costs, and over the average turnover rate for resident relationships. During the first quarter of 2003, the Company acquired its second property in the Boston area with 280 units in Stoughton, MA. The total purchase price of $34,000, including closing costs, equates to approximately $121 per apartment unit. The weighted average expected first year capitalization rate on this acquisition is 7.7%. Capitalization rate ("cap rate") is defined as the rate of interest used to convert the first year expected net operating income ("NOI") less a 3.0% management fee into a single present value. NOI is defined by the Company as rental income and property other income less operating and maintenance expenses. Management generally considers NOI to be an appropriate measure of operating performance because it helps investors to understand the operations of a community. In addition the apartment communities are valued and sold in the market by using a multiple of NOI. During the third quarter of 2003, the Company acquired a 450-unit community in Silver Spring, Maryland. The total purchase price of $58,876, including closing costs, equates to approximately $131 per apartment unit. Management anticipates a 7.1% weighted average expected first year capitalization rate on this acquisition. During the first nine months of 2003, the Company sold five communities with a total of 934 apartment units in Indiana, Ohio, Pennsylvania, Maryland, and Michigan for total consideration of $40,597, or an average of

$43.4 per unit. A gain on sale of approximately $634, net of minority interest, was recorded for the nine-months ended September 30, 2003 from these transactions and is reflected in discontinued operations. Due to the prepayment of debt associated with the sale of two of these communities, a combined $1,610 charge was recorded during the first nine-months. Contractual Obligations and Other Commitments The primary obligations of the Company relate to its mortgage notes payable and its borrowings under the line of credit. The Company's mortgage notes payable and line of credit outstanding at September 30, 2003 and December 31, 2002 are summarized as follows (in thousands): September 30, 2003 December 31, 2002 ----------------- ---------------- Fixed rate mortgage notes payable $1,315,720 $1,279,752 Variable rate mortgage notes payable 30,750 21,055 ---------- ---------- Total mortgage notes payable 1,346,470 1,300,807 Variable rate line of credit facility 64,000 35,000 ---------- ---------- Total mortgage notes payable and line of credit facility $1,410,470 $1,335,807 ========== ========== Mortgage notes payable are collateralized by certain apartment communities and mature at various dates from July, 2004 through June, 2036. The weighted average interest rate of the Company's variable rate notes and credit facility was 2.22% and 2.83% at September 30, 2003 and December 31, 2002, respectively. The weighted average interest rate of the Company's fixed rate notes was 6.45% and 6.50% at September 30, 2003 and December 31, 2002, respectively. The Company has a non-cancelable operating ground lease for one of its properties. The lease expires May 1, 2020, with options to extend the term of the lease for two successive terms of twenty-five years each. At September 30, 2003, future minimum rental payments required under the lease are $70 per year until the lease expires. The lease also provides for contingent rental payments based on collected rents. The contingent rent expense for the nine-month period ended September 30, 2003 amounted to $110. As discussed in the section entitled "Off-Balance Sheet Investments," the Company has the following guarantees or commitments relating to its equity method partnership investments: a) guarantee for a total of $596 of debt associated with two of partnerships, b) guarantee of the low income housing tax credits to the limited partners for a period of five years in 75 partnerships totaling approximately $63.8 million, and c) the obligation to advance funds to meet partnership operating deficits for a five year period for certain partnerships. The Company believes the properties' operations conform to the applicable requirements as set forth above and do not anticipate any payment on these tax credit guarantees. Capital Improvements The Company's policy is to capitalize costs related to the acquisition, development, rehabilitation, construction and improvement of properties. Capital improvements are costs that increase the value and extend the useful life of an asset. Ordinary repair and maintenance costs that do not extend the useful life of the asset are expensed as incurred. Costs incurred on a lease turnover due to normal wear and tear by the resident are expensed on the turn. Recurring capital improvements typically include: appliances, carpeting and flooring, HVAC equipment, kitchen/ bath cabinets, new roofs, site improvements and various exterior building improvements. Non- recurring, revenue generating capital improvements include, among other items: community centers, new windows, and kitchen/ bath apartment upgrades. Revenue generating capital improvements will directly result in rental earnings or expense savings. The Company capitalizes interest and certain internal personnel costs related to the communities under rehabilitation and construction. The Company estimates that on an annual basis $525 per unit is spent on recurring capital expenditures. During the three and nine-month periods ended September 30, 2003 approximately $131 and $393 per unit was estimated to be spent on recurring capital expenditures. The table below summarizes the actual total capital improvements incurred by major categories for the three and nine-month periods ended September 30, 2003 and 2002 and an estimate of the breakdown of total capital improvements by major categories between recurring and non-recurring, revenue generating capital improvements for the three and nine-month periods ended September 30, 2003 as follows: For the three-month period ended September 30, (in thousands, except per unit data) 2003 2002 -- Non- Total Total Recurring Per Recurring Per Capital Per Capital Per Cap Ex Unit(a) Cap Ex Unit(a) Improvements Unit(a) Improvements Unit(a) ------ ------- ------ ------- ----------- ------- ----------- ------- New Buildings $ - $ - $ 530 $13 $ 530 $13 $ 605 $15 Major building improvements 943 23 4,925 119 5,868 142 4,859 124 Roof replacements 360 9 1,582 38 1,942 47 1,353 34 Site improvements 345 8 2,700 65 3,045 73 2,860 73 Apartment upgrades 680 16 9,178 221 9,858 237 9,930 253 Appliances 565 14 793 19 1,358 33 1,349 34 Carpeting/Flooring 1,774 43 2,000 48 3,774 91 3,181 81 HVAC/Mechanicals 523 12 3,984 96 4,507 108 3,836 98 Miscellaneous 233 6 535 14 768 20 850 22 ------- ---- ------- ------ ------- ------ ------- ------ Totals $5,423 $131 $26,227 $633 $31,650 $764 $28,823 $734 ======= ==== ======= ====== ======= ====== ======= ====== (a) Calculated using the weighted average number of units outstanding, including 36,566 core units, 2002 acquisition units of 4,492 and 2003 acquisition units of 385 for the three-month period ended September 30, 2003 and 36,566 core units and 2002 acquisition units of 2,683 for the three-month period ended September 30, 2002. For the nine-month period ended September 30, (in thousands, except per unit data) 2003 2002 -- ----------------------- Non- Total Total Recurring Per Recurring Per Capital Per Capital Per Cap Ex Unit(a) Cap Ex Unit(a) Improvements Unit(a) Improvements Unit(a) ------ ------- ------ ------- ----------- ------- ----------- ------- New Buildings $ - $ - $1,413 $ 34 $1,413 $ 34 $3,614 $ 95 Major building improvements 2,821 68 12,945 313 15,766 381 14,935 392 Roof replacements 1,078 26 2,203 53 3,281 79 3,444 90 Site improvements 1,033 25 4,838 117 5,871 142 8,351 219 Apartment upgrades 2,036 49 23,904 578 25,940 627 24,796 651 Appliances 1,691 41 1,943 47 3,634 88 3,295 87 Carpeting/Flooring 5,308 128 3,768 91 9,076 219 8,020 211 HVAC/Mechanicals 1,564 38 8,490 205 10,054 243 8,585 226 Miscellaneous 694 18 2,085 52 2,779 70 3,020 80 ------- ---- ------- ------ ------- ------ ------- ------ Totals $16,225 $393 $61,589 $1,490 $77,814 $1,883 $78,060 $2,051 ======= ==== ======= ====== ======= ====== ======= ====== (a) Calculated using the weighted average number of units outstanding, including 36,566 core units, 2002 acquisition units of 4,492 and 2003 acquisition units of 272 for the nine-month period ended September 30, 2003 and 36,566 core units and 2002 acquisition units of 1,498 for the nine-month period ended September 30, 2002. The schedule below summarizes the breakdown of total capital improvements between core and non-core as follows: For the three-month period ended September 30, (in thousands, except per unit data) 2003 2002 -- ----------------------- Non- Total Total Recurring Per Recurring Per Capital Per Capital Per Cap Ex Unit(a) Cap Ex Unit(a) Improvements Unit(a) Improvements Unit(a) ------ ------- ------ ------- ----------- ------- ----------- ------- Core Communities $4,785 $131 $19,916 $545 $24,701 $676 $26,556 $ 723 2003 Acquisition Communities 50 131 82 214 132 345 - - 2002 Acquisition Communities 588 131 6,229 1,387 6,817 1,518 2,267 1,546 ------- ---- ------- ------ ------- ------ ------- ------ Sub-total 5,423 131 26,227 633 31,650 764 28,823 754 2003 Disposed Communities 27 131 119 569 146 700 746 799 2002 Disposed Communities - - - - - - 103 1,115 Corporate office expenditures (1) - - - - 869 - 1,019 - ------- ---- ------- ------ ------- ------ ------- ------ $5,450 $131 $26,346 $633 $32,665 $ 764 $30,691 $756 ======= ==== ======= ====== ======= ====== ======= ====== For the nine-month period ended September 30, (in thousands, except per unit data) 2003 2002 -- ----------------------- Non- Total Total Recurring Per Recurring Per Capital Per Capital Per Cap Ex Unit(a) Cap Ex Unit(a) Improvements Unit(a) Improvements Unit(a) ------ ------- ------ ------- ----------- ------- ----------- ------- Core Communities $14,355 $393 $46,635 $1,275 $60,990 $1,668 $74,645 $2,041 2003 Acquisition Communities 107 393 78 287 185 680 - - 2002 Acquisition Communities 1,763 393 14,876 3,312 16,639 3,705 3,415 2,280 ------- ---- ------- ------ ------- ------ ------- ------ Sub-total 16,225 393 61,589 1,490 77,814 1,883 78,060 2,051 2003 Disposed Communities 139 393 263 742 402 1,135 1,661 1,778 2002 Disposed Communities - - - - - - 1,104 1,274 Corporate office expenditures (1) - - - - 1,808 - 3,449 - ------- ---- ------- ------ ------- ------ ------- ------ $16,364 $393 $61,852 $1,484 $80,024 $1,876 $84,274 $2,027 ======= ==== ======= ====== ======= ====== ======= ====== (1) No distinction is made between recurring and non-recurring expenditures for corporate office. Results of Operations Summary of Core Properties The Company had 127 apartment communities with 36,566 units which were owned during the nine-month period being presented (the "Core Properties"). The Company has acquired an additional 22 apartment communities with 5,010 units during 2002 and 2003 (the "Acquired Communities"). In addition, the Company also disposed of 17 properties with a total of 2,658 units during 2002 and 2003 (the "Disposition Communities"). These dispositions have been classified as discontinued operations. The inclusion of the Acquired Communities generally accounted for the significant changes in operating results for the nine-months ended September 30, 2003. A summary of the Core Properties net operating income is as follows (in thousands): Nine Months Three Month ----------- ----------- 2003 2002 %Chg 2003 2002 %Chg ---- ---- ---- ---- ---- ---- Rental income $267,173 $259,285 3.0% $91,018 $88,253 3.1% Property other income 10,828 10,439 3.7% 3,639 3,975 (8.5%) -------- -------- ---- ------ ------- ---- Total income 278,001 269,724 3.1% 94,657 92,228 2.6% Operating and Maintenance (124,169) (114,279) (8.7%) (40,972) (37,315) (9.8%) -------- -------- ---- ------- ------- ---- Net operating income $153,832 $155,445 (1.0%) $53,685 $54,913 (2.2%) ======== ======== ====== ======= ======= ==== Comparison of nine-months ended September 30, 2003 to the same period in 2002 Of the $38,134 increase in rental income, $30,246 is attributable to the Acquired Communities. The balance of this increase, which is from the Core Properties, was the result of an increase of 3.0% in weighted average rental rates, offset by a decrease in occupancy from 92.1% to 92.2%. Occupancy is defined as total possible rental income, net of vacancy and bad debt expense as a percentage of total possible rental income. Total possible rental income is determined by valuing occupied units at contract rates and vacant units at market rents. Property other income, which consists primarily of income from operation of laundry facilities, late charges, administrative fees, garage and carport charges, net profits from corporate apartments, cable revenue, pet charges, and miscellaneous charges to residents increased by $1,018. Of this increase, $629 is attributable to the Acquired Communities and $389 represents a 3.7% increase from the Core Properties. Interest and dividend income decreased $677 due to decreased levels of financing to affiliates and a lower interest rate environment. Of the $22,364 increase in operating and maintenance expenses, $12,474 is attributable to the Acquired Communities. The balance, a $9,890 increase, is attributable to the Core Properties and is primarily due to increases in utility costs, repairs and maintenance, personnel costs, property insurance, and property management costs. The increase in personnel and snow removal costs of $2,768 are significantly related to weather conditions. The regions in which the Company operates, received higher than normal snowfall, and many regions that get very little snow were hit with unusual snow storms. A significant amount of overtime was incurred clearing and shoveling. The increase in repairs and maintenance is primarily due to higher turnover of apartment units in the summer months as property management has actively managed lease expirations so that more leases are terminating in periods of higher traffic. Property insurance increased compared to the same period one year ago due to the benefit the Company continued to receive in the prior year from a legal settlement. General and administrative expense increased in 2003 by $5,613, or 64.1%. General and administrative expenses as a percentage of total revenues were 4.4% for 2003 as compared to 3.1% for 2002. The increase primarily is attributed to the consolidation of the Management Companies in 2003 which added an additional $3,421 to this line item. Previously such expenses were allocated and charged to the Management Companies and were included in the equity in earnings (losses) of unconsolidated affiliates. Of the remaining $2,192 variance, $675 is related to the expensing of stock options for the first time in both of the first three quarters of 2003 and a $1,019 increase in incentive compensation costs compared to the same period a year ago. The balance of this increase is attributable to incremental increases in general and administrative costs related to the 2002 Acquisition Communities. Subsequent to the end of the third quarter, the Company announced that effective January 1, 2004, Norman and Nelson Leenhouts were retiring as Co-CEO's and Edward Pettinella will become President and CEO. In recognition of the value created under their leadership, Norman and Nelson received restricted stock grants with a combined value of approximately $5 million. A one time, non-recurring charge equal to this $5 million will be recorded in the fourth quarter of 2003 and included in general and administrative expense. In addition, the Company announced that on January 1, 2004, the commercial property management division of Home Properties will be sold to Home Leasing LLC, which is owned by Norman and Nelson Leenhouts, in order to avoid conflicts of interest and focus Home Properties solely on the direct ownership and management of market rate apartment communities. The commercial property management division consists of the business of managing under contract six commercial properties, three single-family land developments and one affordable multifamily apartment community. The majority of these properties were all managed by Home Leasing Corporation, also owned by Norman and Nelson Leenhouts, prior to the Companies IPO. The right to manage these properties would revert to Home Leasing Corporation for no consideration upon termination of the Leenhoutses' employment on December 31, 2006. The consideration to be paid is $68 plus a percentage of the management fee received by Home Leasing in connection with the management of one of the commercial properties for so long as the management of that property is retained. If Home Leasing continues to manage that property for three years, the consideration would increase $166. This division currently contributes approximately $130 annually to operations. The revenue from this division is reflected in other income and the majority of the expenses are included in general and administrative. Interest expense increased $7,914 due to the increase in the amount of debt outstanding associated with the Acquired Communities offset in part by lower interest rates. Due to the prepayment of debt associated with the sale of Candlewood Apartments in Indiana during the first quarter, and Bayberry Place Apartments in Michigan during the third quarter, a $1,610 charge was recorded for the nine-months ended September 30, 2003. Depreciation and amortization expense increased $10,724 due to the depreciation on the Acquisition Communities, the additions to the Core Properties, net of the Disposition Communities. In the fourth quarter of 2002, the Company announced its intention to sell virtually all of the assets associated with its general partner interests in the affordable properties to focus solely on the direct ownership and management of market rate apartment communities. At that time, the Company announced its intention to sell the assets, which include principally loans, advances and management contracts. During the first nine-months of 2003, the Company recorded impairment charges of $2,408. Of this total, $712 represents advances made to certain of the affordable property limited partnerships during the first nine months of 2003 which the Company believes will not be repaid upon the sale of the loans. The remaining $1,696 pertains to an additional net impairment charge taken on Phase III to reduce the assets to fair market value. The equity in earnings (losses) of unconsolidated affiliates of $1,497 is primarily the result of the general partner recording a greater share of the underlying investment's losses due to the loans and advances to certain of the affordable property limited partnerships where the limited partner has no capital account. This is pursuant to the accounting requirements of EITF 99-10, "Percentage Used to Determine the Amount of Equity Method Losses." Included and classified in the account are $691 of advances made during the first nine months of 2003 which the Company believes will not be repaid upon sale of the loans. Minority interest decreased $2,030 due to the impairment of assets held by the General Partner recorded in the first nine months of 2003 together with an overall reduction in income from operations as a result of increased interest and depreciation costs as compared to the previous period. Both of these items were offset by the impact of the premium paid on the repurchase of the Series B Convertible Cumulative Preferred Stock which had been treated as a charge to net income available to common shareholders in the previous year. Included in discontinued operations for the nine-month period ended September 30, 2002 are seventeen apartment community dispositions (five and twelve sold in 2003 and 2002, respectively) and five properties sold in 2003 for the nine-month period ended September 30, 2003 and one property held for sale for both the nine-month periods ended September 30, 2003 and 2002. The operations of these seventeen properties have been reflected on a comparative basis for the period ended September 30, 2002. The Company reported a $245 loss, net of minority interest, on disposition of property in the first quarter of 2002 relating to additional expenses incurred in the same quarter for a sale which closed in the fourth quarter of 2001. These costs represented a change in estimate from those accrued at the time of sale. Comparison of the three-months ended September 30, 2003 to the same period in 2002 Of the $10,134 increase in rental income, $7,369 is attributable to the Acquired Communities. The balance of this increase, which is from the Core Properties, was the result of an increase of 3.1% in weighted average rental rates. Occupancy reflected a slight increase and was 93.3%, up from 93.2% for the same period a year ago. Occupancy is defined as total possible rental income, net of vacancy and bad debt expense as a percentage of total possible rental income. Total possible rental income is determined by valuing occupied units at contract rates and vacant units at market rents. Property other income, which consists primarily of income from operation of laundry facilities, late charges, administrative fees, garage and carport charges, net profits from corporate apartments, cable revenue, pet charges, and miscellaneous charges to residents decreased by $142. Of this decrease, $194 is attributable to an increase from the Acquired Communities and $336 represents an 8.5% decrease from the Core Properties. Interest and dividend income decreased $181 due to decreased levels of financing to affiliates and a lower interest rate environment. Of the $6,549 increase in operating and maintenance expenses, $2,892 is attributable to the Acquired Communities. The balance, a $3,657 increase, is attributable to the Core Properties and is primarily due to increases in repairs and maintenance, advertising, property insurance and allocated property management costs. A significant amount of the increase in both repairs and maintenance and advertising expense relates to increased turnover during June, July, and August. This is a result of actively managing lease expirations to better match lease termination dates with higher traffic periods. Property insurance expenses in 2002 continued to benefit from the legal settlement received a couple of years ago. General and administrative expense increased in 2003 by $1,833, or 64.6%. General and administrative expenses as a percentage of total revenues were 4.2% for 2003 as compared to 2.8% for 2002. The increase primarily is attributed to the consolidation of the Management Companies in 2003 which added an additional $1,151 to this line item. Previously such expenses were allocated and charged to the Management Companies and were included in the equity in earnings (losses) of unconsolidated affiliates. The primary contributors to the remaining $682 variance are $266 related to the expensing of stock options for the first time in the third quarter of 2003 and a $258 increase in incentive compensation costs compared to the same period a year ago. Interest expense increased $1,743 due to the increase in the amount of debt outstanding associated with the Acquired Communities offset in part by lower interest rates. Due to the prepayment of debt associated with the sale of Bayberry Place Apartments in Michigan during the third quarter, a $261 charge was recorded during the three-months ended September 30, 2003. Depreciation and amortization expense increased $2,984 due to the depreciation on the Acquisition Communities and the additions to the Core Properties. In the fourth quarter of 2002, the Company announced its intention to sell virtually all of the assets associated with its general partner interests in the affordable properties to focus solely on the direct ownership and management of market rate apartment communities. At that time, the Company announced its intention to sell the assets, which include principally loans, advances and management contracts. During the third quarter of 2003, the Company recorded impairment charges of $1,888. Of this total, $192 represents advances made to certain of the affordable property limited partnerships during the third quarter which the Company believes will not be repaid upon the sale of the loans. The remaining $1,696 pertains to an additional net impairment charge taken on Phase III to reduce the assets to fair market value. The equity in earnings (losses) of unconsolidated affiliates of $313 is primarily the result of the general partner recording a greater share of the underlying investment's losses due to the loans and advances to certain of the affordable property limited partnerships where the limited partner has no capital account. This is pursuant to the accounting requirements of EITF 99-10, "Percentage Used to Determine the Amount of Equity Method Losses." Included and classified in the account are $345 of advances made during the third quarter of 2003 which the Company believes will not be repaid upon sale of the loans. Minority interest decreased $1,615 due to the impairment of assets held by the General Partner recorded in the third quarter of 2003 together with an overall reduction in income from operations as a result of increased interest and depreciation costs as compared to the previous period. Included in discontinued operations for the three-month period ended September 30, 2002 are seventeen apartment community dispositions (five and twelve sold in 2003 and 2002, respectively) and five properties sold in 2003 for the three-month period ended September 30, 2003 and one property held for sale for both the three-month periods ended September 30, 2003 and 2002. The operations of these seventeen properties have been reflected on a comparative basis for the period ended September 30, 2002. Funds From Operations Pursuant to the revised definition of Funds From Operations ("FFO") adopted by the Board of Governors of the National Association of Real Estate Investment Trusts ("NAREIT"), FFO is defined as net income (computed in accordance with accounting principles generally accepted in the United States of America ("GAAP")) excluding gains or losses from sales of property, minority interest and extraordinary items plus depreciation from real property including adjustments for unconsolidated partnerships and joint ventures less dividends from non-convertible preferred shares. The Company considers debt extinguishment costs which are incurred as a result of repaying property specific debt and non-cash real estate impairment charges, as a component of the gain or loss on sale of the property. Because of the limitations of the FFO definition as published by NAREIT as set forth above, the Company has made certain interpretations in applying the definition. The Company believes all adjustments not specifically provided for are consistent with the definition. Management believes that in order to facilitate a clear understanding of the combined historical operating results of the Company, FFO should be considered in conjunction with net income as presented in the consolidated financial statements included elsewhere herein. Management believes that by excluding gains or losses related to dispositions of property and excluding real estate depreciation (which can vary among owners of similar assets in similar condition based on historical cost accounting and useful life estimates), FFO can help one compare the operating performance of a company's real estate between periods or as compared to different companies. FFO does not represent cash generated from operating activities in accordance with generally accepted accounting principles and is not necessarily indicative of cash available to fund cash needs. Cash provided by operating activities was $108,533 and $105,995 for the nine-month period ended and $32,230 and $32,847 for the three-month period ended September 30, 2003 and 2002, respectively. Cash used in investing activities was $102,139 and $222,320 for the nine-month period ended and $45,432 and $47,975 for the three-month period ended September 30, 2003 and 2002, respectively. Cash (used in) and provided by financing activities was ($7,925) and $113,420 for the nine-month period ended and $13,743 and $10,203 for the three-month period ended September 30, 2003 and 2002, respectively. FFO should not be considered as an alternative to net income as an indication of the Company's performance or to cash flow as a measure of liquidity. The calculation of FFO and reconciliation to GAAP net income available to common shareholders for the nine and three-months ended September 30, 2003 and 2002 are presented below (in thousands): Nine Months Three Months ----------- ------------ 2003 2002 2003 2002 ---- ---- ---- ---- Net income available to common shareholders $21,772 $29,408 $ 8,958 $13,063 Convertible preferred dividends 5,306 8,222 1,296 2,443 Minority interest 11,935 13,965 4,776 6,391 Minority interest - income (loss) from discontinued operations 105 868 95 (271) Depreciation from real property 56,889 48,626 19,512 17,020 Depreciation from real property from unconsolidated entities 1,837 505 725 68 Impairment of real property included in income from operations of disposed properties, before minority interest 423 1,565 - 1,565 Impairment on General Partner real estate investment 1,785 - 1,785 - Loss on disposition of property 79 245 69 - Prepayment penalty from early extinguishment of debt in connection with sale of real estate 1,610 - 261 - (Gain) loss on disposition of discontinued operations, net of minority interest (355) (5,601) (35) (2,912) -------- -------- -------- -------- FFO as defined above 101,386 97,803 37,442 37,367 Premium on Series B preferred stock repurchase - 5,025 - - -------- -------- -------- -------- FFO as adjusted by the Company $101,386 $102,828 $37,442 $37,367 ======== ======== ======== ======== Weighted average common shares/units outstanding: - Basic 44,577.3 41,739.9 45,611.9 42,364.2 ======== ======== ======== ======== - Diluted 47,624.0 46,370.1 48,078.9 46,367.7 ======== ======== ======== ======== On May 24, 2002 the Company repurchased the 1.0 million shares outstanding of the Series B preferred stock at an amount equivalent to 839,772 common shares (as if the preferred shares had been converted). The stock had a liquidation preference of $25.00 per share, a conversion price of $29.77 per share, and a five-year, non-call provision. The Company repurchased the shares for $29,392 equal to the $35.00 common stock trading price when the transaction was consummated. A premium of $5,025 was incurred on the repurchase. In the adjusted presentation above, the Company excluded the premium on the Series B preferred stock. The Company believes that this calculation is more reflective of continuing operations as the premium was considered a one time charge. All REITs may not be using the same definition for FFO. Accordingly, the above presentation may not be comparable to other similarly titled measures of FFO of other REITs. Covenants In connection with the issuance of the Series F Preferred Stock, the Company is required to maintain for each fiscal quarterly period a fixed charge coverage ratio, as defined in the Series F Cumulative Redeemable Preferred Stock Article Supplementary, of 1.75 to 1.0. The fixed charge coverage ratio and the components thereof do not represent a measure of cash generated from operating activities in accordance with generally accepted accounting principles and are not necessarily indicative of cash available to fund cash needs. Further, this ratio should not be considered as an alternative measure to net income as an indication of the Company's performance or of cash flow as a measure of liquidity. The calculation of the fixed charge coverage ratio for the four most recent quarters since the issuance of the Series F Preferred Stock are presented below (in thousands). Net operating income from discontinued operations in the calculation below is defined as total revenues from discontinued operations less operating and maintenance expenses. Calculation Presented for Series F Covenants Three-months ended Sept. 30 June 30 Mar. 31 Dec. 31 2003 2003 2003 2002 ---- ---- ---- ---- EBITDA Total revenues $111,200 $109,713 $106,955 $105,715 Net operating income from discontinued operations 460 - 196 299 Operating and maintenance (46,472) (46,040) (49,772) (44,199) General and administrative (4,670) (4,582) (5,119) (3,891) Impairment of assets held as General Partner (1,888) (93) (427) (3,183) Equity in earnings (losses) of unconsolidated affiliates (313) (444) (740) (16,085) -------- -------- -------- -------- $ 58,317 $ 58,554 $ 51,093 $ 38,656 Fixed Charges Interest expense $ 21,456 $ 21,634 $ 21,300 $ 20,350 Interest expense on discontinued operations 116 - 33 - Preferred dividends 2,646 3,192 3,518 3,717 Capitalized interest 230 230 230 230 -------- -------- -------- -------- $ 24,448 $ 25,056 $ 25,081 $ 24,297 Times Coverage ratio: 2.39 2.34 2.04 1.59(1) (1) Results for the quarter reflect impairment and other charges relating to certain government assisted properties ("affordable properties") in which the Company is a general partner as described in more detail in the notes to the Company's annual report filed on form 10K. Excluding the impairment and other charges of $18,074, the fixed charge coverage ratio would have been 2.34. Economic Conditions Substantially all of the leases at the Company's apartment communities are for a term of one year or less, which enables the Company to seek increased rents upon renewal of existing leases or commencement of new leases. These short-term leases minimize the potential adverse effect of inflation on rental income, although residents may leave without penalty at the end of their lease terms and may do so if rents are increased significantly. Historically, real estate has been subject to a wide range of cyclical economic conditions, which affect various real estate sectors and geographic regions with differing intensities and at different times. In 2002 and continuing into 2003 many regions of the United States have experienced varying degrees of economic recession and certain recessionary trends, such as the cost of obtaining sufficient property and liability insurance coverage, short-term interest rates, and a temporary reduction in occupancy. In light of this, we will continue to review our business strategy however, we believe that given our property type and the geographic regions in which we are located, we do not anticipate any changes in our strategy or material effects in financial performance. Declaration of Dividend On October 28, 2003, the Board of Directors approved a dividend of $.61 per share for the quarter ended September 30, 2003. This is the equivalent of an annual distribution of $2.44 per share. The dividend is payable November 25, 2003 to shareholders of record on November 14, 2003. On October 28, 2003 the Company also declared a regular dividend of $0.5625 per share on its Series F Cumulative Redeemable Preferred Stock, for the quarter ending November 30, 2003. The dividend on the preferred shares is payable on December 1, 2003, to shareholders of record on November 14, 2003. This dividend is equivalent to an annualized rate of $2.25 per share. Contingency In 2001, the Company underwent a state tax audit. The state has assessed taxes of $469 for the 1998 and 1999 tax years under audit. If the state's position is applied to all tax years through December 31, 2001, the assessment would be $1.3 million. At the time, the Company believed the assessment and the state's underlying position was not supportable by the law nor consistent with previously provided interpretative guidance from the office of the State Secretary of Revenue. After two subsequent enactments by the state legislature during 2002 affecting the pertinent tax statute, the Company has been advised by its third party legal counsel that its filing position for 1998-2001 should prevail. Based upon this information as of September 30, 2003, the Company has recorded an accrual of $525, representing only its 2002 liability. Effective January 1, 2003, the Company reorganized the ownership of Home Properties Trust, subjecting the Company to a much lower level of tax going forward. New Accounting Standard In January 2003, the FASB issued Interpretation No. 46 - "Consolidation of Variable Interest Entities", an interpretation of ARB No. 51 - "Consolidated Financial Statements." The interpretation addresses consolidation by businesses of special purpose entities (variable interest entities, "VIE"). This interpretation addresses consolidation by business enterprises of variable interest entities in which the equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support from other parties or in which the equity investors do not have the characteristics of a controlling financial interest. This interpretation requires a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. The interpretation also requires disclosures about variable interest entities that the company is not required to consolidate but in which it has a significant variable interest. The consolidation requirements of this interpretation apply immediately to variable interest entities created after January 31, 2003 but a deferral has been granted until the end of the first fiscal year or interim period ending after December 15, 2003 for VIE's existing before February 1, 2003. Therefore it is effective on December 31, 2003 for the Company. Management is uncertain but is assuming it is reasonably possible that each of the limited partnerships in which it holds the general partnership interest as of December 31, 2003 would be considered a VIE. The Company is determining where it is the primary beneficiary, and as a result the Company may consolidate all or a certain number of the limited partnership's assets and liabilities. In April 2003, the FASB issued SFAS No. 149 "Amendment of Statement 133 on Derivative Instruments and Hedging Activities". This Statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." This Statement is effective for contracts entered into or modified after June 30, 2003. The provisions of FAS 149 are not expected to have a material impact on the Company's financial statements. In May 2003, FASB issued SFAS 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity." This Statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). This Statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. On October 29, 2003 the FASB indefinitely deferred the provisions of paragraphs 9 and 10 of SFAS 150 as they apply to mandatorily redeemable noncontrolling interests. This deferral applies to minority interest ownerships in limited partnerships which are mandatorily redeemable upon termination of the partnership and therefore is potentially applicable to the affordable portfolio. HOME PROPERTIES, INC. ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK The Company's primary market risk exposure is interest rate risk. At September 30, 2003 and December 31, 2002, approximately 93% and 96%, respectively, of the Company's debt bore interest at fixed rates with a weighted average maturity of approximately 8 years and a weighted average interest rate of approximately 6.45% and 6.50%, respectively. The remainder of the Company's debt bears interest at variable rates with a weighted average maturity of approximately 9 and 2 years, respectively, and a weighted average interest rate of 2.22% and 2.83%, respectively, at September 30, 2003 and December 31, 2002. The Company does not intend to utilize a significant amount of variable rate debt to acquire properties in the future. On occasion, the Company may assume variable rate debt in connection with a property acquisition. The Company believes, however, that in no event would increases in interest expense as a result of inflation significantly impact the Company's distributable cash flow. At September 30, 2003 and December 31, 2002, the interest rate risk on $25.2 million of such variable rate debt has been mitigated through the use of interest rate swap agreements (the "Swaps") with major financial institutions. The Company is exposed to credit risk in the event of non-performance by the counter-parties to the Swaps. The Company believes it mitigates its credit risk by entering into these Swaps with major financial institutions. The Swaps effectively convert an aggregate of $25.2 million in variable rate mortgages to fixed rates of 5.91%, 8.22% and 8.40%. For both September 30, 2003 and December 31, 2002, the fair value of the Company's fixed rate debt, including the $25.2 million which was swapped to a fixed rate, amounted to a liability of $1.4 billion compared to its carrying amount of $1.3 billion. The Company estimates that a 100 basis point decrease in market interest rates at September 30, 2003 would have changed the fair value of the Company's fixed rate debt to a liability of $1.5 billion. The Company intends to continuously monitor and actively manage interest costs on its debt portfolio and may enter into swap positions based upon market fluctuations. In addition, the Company believes that it has the ability to obtain funds through additional equity offerings or the issuance of UPREIT Units. Accordingly, the cost of obtaining such interest rate protection agreements in relation the Company's access to capital markets will continue to be evaluated. The Company has not, and does not plan to, enter into any derivative financial instruments for trading or speculative purposes. As of September 30, 2003, the Company had no other material exposure to market risk. HOME PROPERTIES, INC. ITEM 4. INTERNAL CONTROLS The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's Co-Chief Executive Officers and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Also, the Company has investments in certain unconsolidated entities. As the Company does not control these entities, the disclosure controls with respect to such entities are necessarily substantially more limited than those maintained with respect to the Company's consolidated subsidiaries. The Co-Chief Executive Officers and Chief Financial Officer have, as of the end of the period covered by this quarterly report, evaluated the effectiveness of the disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) and have determined that such disclosure controls and procedures are adequate. In connection with the evaluation, no change in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended) was identified that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting. PART II - OTHER INFORMATION HOME PROPERTIES, INC. Item 6. Exhibits and Reports or Form 8-K (a) Exhibit 31.1 Section 302 Certifications of Chief Executive Officers Exhibit 31.2 Section 302 Certification of Chief Financial Officer Exhibit 32.1 Section 906 Certifications of Chief Executive Officers Exhibit 32.2 Section 906 Certification of Chief Financial Officer (b) Reports on Form 8-K: - Form 8-K was filed on October 29, 2003, date of report October 29, 2003, with respect to Items 5 and 7 disclosures regarding the Registrant's press release announcing the Board of Directors appointment of Edward J. Pettinella, President and Chief Executive Officer of the Registrant effective January 1, 2004. The Registrant also reported that the Board of Directors granted each of Nelson and Norman Leenhouts restricted stock awards having an approximate value of $2.5 million in recognition of their contributions to the Registrant. Finally, the Registrant reported that it has agreed in principle that, on January 1, 2004, the commercial property management division of the Registrant will be sold to Home Leasing LLC, which is owned by Nelson and Norman Leenhouts. - Form 8-K was filed on October 31, 2003, date of report October 31, 2003, with respect to Items 7 and 12 disclosures regarding the Registrant's press release announcing its results for the third quarter of 2003 and the third quarter 2003 investor conference call. SIGNATURES Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. HOME PROPERTIES, INC. (Registrant) Date: November 14, 2003 By: /s/ Norman P. Leenhouts --- Norman P. Leenhouts Chairman and Co-Chief Executive Officer Date: November 14, 2003 By: /s/ David P. Gardner --- David P. Gardner Senior Vice President and Chief Financial Officer