ENTERTAINMENT PROPERTIES TRUST
Form 10-Q
April 26, 2007

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2007

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES ACT OF 1934**

For the transition period from __________ to __________

Commission File Number: 1-13561

ENTERTAINMENT PROPERTIES TRUST

(Exact name of registrant as specified in its charter)

Maryland	**43-1790877**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
30 West Pershing Road, Suite 201 Kansas City, Missouri	**64108**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **(816) 472-1700**

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 þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No þ

At April 24, 2007, there were 26,651,870 Common Shares of beneficial interest outstanding.

Table of Contents

FORWARD LOOKING STATEMENTS

Certain statements contained or incorporated by reference herein constitute forward-looking statements as such term is defined in Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). The forward-looking statements may refer to financial condition, results of operations, plans, objectives, future financial performance and business of the Company. Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Our future results, financial condition and business may differ materially from those expressed in these forward-looking statements. You can find many of these statements by looking for words such as approximates, believes, expects, anticipates, estimates, intends, plans would, may or other similar expressions in this Report on Form 10-Q. In addition, references to our budgeted amounts are forward looking statements. These forward-looking statements represent our intentions, plans, expectations and beliefs and are subject to numerous assumptions, risks and uncertainties. Many of the factors that will determine these items are beyond our ability to control or predict. For further discussion of these factors see Item 1A. Risk Factors in the Annual Report on Form 10-K for the year ended December 31, 2006 filed with the SEC on February 28, 2007.

For these statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. You are cautioned not to place undue reliance on our forward-looking statements, which speak only as of the date of this Quarterly Report on Form 10-Q or the date of any document incorporated by reference. All subsequent written and oral forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. We do not undertake any obligation to release publicly any revisions to our forward-looking statements to reflect events or circumstances after the date of this Quarterly Report on Form 10-Q.

TABLE OF CONTENTS

		Page
PART I		4
Item 1.	Financial Statements	4
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	17
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	27
Item 4.	Controls and Procedures	28
PART II		29
Item 1.	Legal Proceedings	29
Item 1A.	Risk Factors	29
Item 2.	Unregistered Sale of Equity Securities and Use of Proceeds	29
Item 3.	Defaults Upon Senior Securities	30
Item 4.	Submission of Matter to a Vote of Security Holders	30
Item 5.	Other Information	30
Item 6.	Exhibits	30

Certification of Chief Executive Officer
Certification of Chief Financial Officer
Section 1350 Certification
Section 1350 Certification

Table of Contents

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

ENTERTAINMENT PROPERTIES TRUST
Consolidated Balance Sheets
(Dollars in thousands, except share data)

	March 31, 2007 (Unaudited)	December 31, 2006
Assets		
Rental properties, net of accumulated depreciation of $149.5 million and $141.6 million at March 31, 2007 and December 31, 2006, respectively	$ 1,399,761	$ 1,395,903
Property under development	26,480	19,272
Mortgage notes and related accrued interest receivable	115,278	76,093
Investment in joint ventures	2,156	2,182
Cash and cash equivalents	6,755	9,414
Restricted cash	7,168	7,365
Intangible assets, net	9,165	9,366
Deferred financing costs, net	9,981	10,491
Accounts and notes receivable	35,128	30,043
Other assets	12,454	11,150
Total assets	$ 1,624,326	$ 1,571,279
Liabilities and Shareholders Equity		
Liabilities:		
Accounts payable and accrued liabilities	$ 8,170	$ 16,480
Common dividends payable	20,253	18,204
Preferred dividends payable	4,856	3,110
Unearned rents	552	1,024
Long-term debt	734,456	675,305
Total liabilities	768,287	714,123
Minority interests	4,341	4,474
Shareholders equity:		
Common Shares, $.01 par value; 50,000,000 shares authorized; and 27,425,635 and 27,153,411 shares issued at March 31, 2007 and December 31, 2006, respectively	274	272
Preferred Shares, $.01 par value; 15,000,000 shares authorized:		
2,300,000 Series A shares issued at March 31, 2007 and December 31, 2006; liquidation preference of $57,500,000	23	23
3,200,000 Series B shares issued at March 31, 2007 and December 31, 2006; liquidation preference of $80,000,000	32	32
5,400,000 Series C convertible shares issued at March 31, 2007 and December 31, 2006; liquidation preference of $135,000,000	54	54

Additional paid-in-capital				
Treasury shares at cost: 776,505 and 675,487 common shares		890,046		883,639
at March 31, 2007 and December 31, 2006, respectively		(21,919)		(15,500)
Loans to shareholders		(3,525)		(3,525)
Accumulated other comprehensive income		13,726		12,501
Distributions in excess of net income		(27,013)		(24,814)
Shareholders equity		851,698		852,682
Total liabilities and shareholders equity	$	1,624,326	$	1,571,279

See accompanying notes to consolidated financial statements.

4

Table of Contents

ENTERTAINMENT PROPERTIES TRUST
Consolidated Statements of Income
(Unaudited)
(Dollars in thousands, except share data)

	Three Months Ended March 31,	
	2007	**2006**
Rental revenue	$ 42,965	$ 39,473
Tenant reimbursements	3,642	3,450
Other income	781	1,463
Mortgage financing interest	3,022	1,824
Total revenue	50,410	46,210
Property operating expense	4,611	4,770
Other operating expense	606	1,038
General and administrative expense	3,232	2,481
Costs associated with loan refinancing		673
Interest expense, net	10,952	11,239
Depreciation and amortization	8,297	7,497
Income before gain on sale of land and income from joint ventures	22,712	18,512
Gain on sale of land		345
Equity in income from joint ventures	198	184
Net income	$ 22,910	$ 19,041
Preferred dividend requirements	(4,856)	(2,916)
Net income available to common shareholders	$ 18,054	$ 16,125
Net income per common share:		
Basic	$ 0.69	$ 0.63
Diluted	$ 0.67	$ 0.62
Shares used for computation (in thousands):		
Basic	26,282	25,690
Diluted	26,820	26,030
Dividends per common share	$ 0.7600	$ 0.6875

See accompanying notes to consolidated financial statements.

5

Table of Contents

ENTERTAINMENT PROPERTIES TRUST
Consolidated Statement of Changes in Shareholders Equity
Three Months Ended March 31, 2007
(Unaudited)
(Dollars in thousands, except share data)

	Common Stock		Preferred Stock		Additional paid-in	Treasury	Loans to	Accumulated other comprehensive income	Distributions in excess of net	
	Shares	Par	Shares	Par	capital	shares	shareholders	(loss)	income	Total
Balance at December 31, 2006	27,153	$ 272	10,900	$ 109	$ 883,639	$ (15,500)	$ (3,525)	$ 12,501	$ (24,814)	$ 852,682
Issuance of restricted shares, including restricted shares issued for payment of bonuses	129	1			1,334					1,335
Amortization of restricted shares					634					634
Share option expense					107					107
Foreign currency translation adjustment								1,400		1,400
Unrealized loss on derivatives								(175)		(175)
Net income									22,910	22,910
Purchase of 24,740 common shares for treasury in conjunction with vesting of employees restricted stock						(1,448)				(1,448)
Issuances of common shares in Dividend	4				197					197

Reinvestment Plan										
Stock option exercises, net	140	1			4,135	(4,971)				(835)
Dividends to common shareholders ($0.76 per share)									(20,253)	(20,253)
Dividends to Series A preferred shareholders ($0.5938 per share)									(1,366)	(1,366)
Dividends to Series B preferred shareholders ($0.4844 per share)									(1,550)	(1,550)
Dividends to Series C preferred shareholders ($0.3594 per share)									(1,940)	(1,940)
Balance at March 31, 2007	27,426	$ 274	10,900	$ 109	$ 890,046	$ (21,919)	$ (3,525)	$ 13,726	$ (27,013)	$ 851,698

See accompanying notes to financial statements.

Table of Contents

ENTERTAINMENT PROPERTIES TRUST
Consolidated Statements of Comprehensive Income
(Unaudited)
(Dollars in thousands)

	Three Months Ended March 31, 2007	Three Months Ended March 31, 2006
Net income	$ 22,910	$ 19,041
Other comprehensive income (loss):		
Foreign currency translation adjustment	1,400	(764)
Unrealized loss on derivatives	(175)	
Comprehensive income	$ 24,135	$ 18,277

See accompanying notes to consolidated financial statements.

Table of Contents

ENTERTAINMENT PROPERTIES TRUST
Consolidated Statements of Cash Flows
(Unaudited)
(Dollars in thousands)

	Three Months Ended March 31, 2007	Three Months Ended March 31, 2006
Operating activities:		
Net income	$ 22,910	$ 19,041
Adjustments to reconcile net income to net cash provided by operating activities:		
Gain on sale of land		(345)
Costs associated with loan refinancing (non-cash portion)		673
Equity in income from joint ventures	(198)	(184)
Depreciation and amortization	8,297	7,497
Amortization of deferred financing costs	662	768
Share-based compensation expense to management and trustees	781	666
Increase in mortgage notes accrued interest receivable	(2,745)	(1,809)
Increase in accounts receivable	(23)	(1,343)
Increase in other assets	(1,379)	(128)
Increase (decrease) in accounts payable and accrued liabilities	(331)	380
Decrease in unearned rents	(472)	(194)
Net cash provided by operating activities	27,502	25,022
Investing activities:		
Acquisition of rental properties and other assets	(16,725)	(38,462)
Net proceeds from sale of real estate		603
Additions to properties under development	(7,433)	(7,097)
Distributions from joint ventures	224	213
Investment in promissory note receivable	(5,000)	(3,500)
Investment in mortgage notes receivable	(35,921)	(15,332)
Net cash used in investing activities	(64,855)	(63,575)
Financing activities:		
Proceeds from long-term debt facilities	100,415	135,196
Principal payments on long-term debt	(42,095)	(121,912)
Deferred financing fees paid	(142)	(2,114)
Net proceeds from issuance of common shares	197	46,389
Impact of stock option exercises, net	(835)	
Purchase of common shares for treasury in conjunction with vesting of employees restricted stock	(1,448)	(919)
Distributions paid to minority interests	(133)	(133)
Dividends paid to shareholders	(21,314)	(18,686)
Net cash provided by financing activities	34,645	37,821
Effect of exchange rate changes on cash	49	(26)

Net decrease in cash and cash equivalents		(2,659)		(758)
Cash and cash equivalents at beginning of year		9,414		6,546
Cash and cash equivalents at end of year	$	6,755	$	5,788
Supplemental schedule of non-cash activity:				
Transfer of property under development to rental property	$	264	$	4,774
Issuance of restricted shares, including restricted shares issued for payment of bonuses	$	8,402	$	3,441
Supplemental disclosure of cash flow information:				
Cash paid during the year for interest	$	11,015	$	11,031
Cash paid during the year for income taxes	$	317	$	224

See accompanying notes to consolidated financial statements.

Table of Contents

ENTERTAINMENT PROPERTIES TRUST
Notes to Consolidated Financial Statements (Unaudited)

1. Organization

Description of Business

Entertainment Properties Trust (the Company) is a Maryland real estate investment trust (REIT) organized on August 29, 1997. The Company was formed to acquire and develop megaplex theatres, entertainment retail centers (centers generally anchored by an entertainment component such as a megaplex theatre and containing other entertainment-related properties), and destination recreational and specialty properties. The Company s properties are located in the United States and Canada.

2. Significant Accounting Policies

Basis of Presentation

The accompanying unaudited consolidated financial statements of the Company have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and revenues and expenses for the period. Actual results could differ significantly from those estimates. In addition, operating results for the three-month period ended March 31, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007.

The consolidated balance sheet as of December 31, 2006 has been derived from the audited consolidated balance sheet at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006 filed with the SEC on February 28, 2007.

Revenue Recognition

Rents that are fixed and determinable are recognized on a straight-line basis over the minimum terms of the leases. Base rent escalation in those of the Company s leases that are dependent upon increases in the Consumer Price Index (CPI) is recognized when known. Straight-line rent receivable is included in accounts receivable and was $17.1 million and $16.4 million at March 31, 2007 and December 31, 2006, respectively. In addition, most of the Company s tenants are subject to additional rents if gross revenues of the properties exceed certain thresholds defined in the lease agreements (percentage rents). Percentage rents are recognized at the time when specific triggering events occur as provided by the lease agreements. Percentage rents of $474 thousand and $469 thousand were recognized during the three months ended March 31, 2007 and 2006, respectively. Lease termination fees are recognized when the related leases are canceled and the Company has no obligation to provide services to such former tenants. No termination fees were recognized during the three months ended March 31, 2007 and 2006.

Table of Contents

Concentrations of Risk

American Multi-Cinema, Inc. (AMC) is the lessee of a substantial portion (53%) of the megaplex theatre rental properties held by the Company (including joint venture properties) at March 31, 2007 as a result of a series of sale leaseback transactions pertaining to a number of AMC megaplex theatres. A substantial portion of the Company s rental revenues (approximately $23.3 million, or 54%, and $23.0 million, or 58%, for the three months ended March 31, 2007 and 2006, respectively) result from the rental payments by AMC under the leases, or its parent, AMC Entertainment, Inc. (AMCE), as the guarantor of AMC s obligations under the leases. AMCE has publicly held debt and accordingly, its consolidated financial information is publicly available.

For the three months ended March 31, 2007 and 2006, respectively, approximately $8.0 million, or 16%, and $7.7 million, or 17%, of total revenue was derived from the Company s four entertainment retail centers in Ontario, Canada. For the three months ended March 31, 2007 and 2006, respectively, approximately $10.6 million, or 21%, and $9.5 million, or 21%, of our total revenue was derived from the Company s four entertainment retail centers in Ontario, Canada combined with the mortgage financing interest related to the Company s mortgage note receivable held in Canada and initially funded on June 1, 2005. The Company s wholly owned subsidiaries that hold the Canadian entertainment retail centers, third party debt and mortgage note receivable represent approximately $166.5 million or 19.5% and $164.0 million or 19.2% of the Company s net assets as of March 31, 2007 and December 31, 2006, respectively.

Share-Based Compensation

The Company accounts for share based compensation under the Financial Accounting Standard (SFAS) No. 123R Share-Based Payment. Share based compensation expense consists of share option expense, amortization of restricted share grants and shares issued to trustees for payment of their annual retainers. Share based compensation is included in general and administrative expense in the accompanying consolidated statements of income, and totaled $781 thousand and $666 thousand for the three months ended March 31, 2007 and 2006, respectively.

Share Options

The fair value of share options granted under the Company s Share Incentive Plan is estimated at the date of grant using the Black-Scholes option pricing model. Awards under the Company s plan vest either immediately or up to a period of 5 years. Share option expense for all options is recognized on a straight-line basis over the vesting period. The expense related to share options included in the determination of net income for the three months ended March 31, 2007 and 2006 was $107 thousand and $66 thousand, respectively. The following assumptions were used in applying the Black-Sholes option pricing model at the grant dates: risk-free interest rate of 4.8% for both the three months ended March 31, 2007 and 2006, dividend yield of 5.4% and 5.8% for the three months ended March 31, 2007 and 2006, respectively, volatility factors in the expected market price of the Company s common shares of 19.5% and 21.1% for the three months ended March 31, 2007 and 2006, respectively; and an expected life of eight years.

Restricted Shares

The Company grants restricted shares to employees pursuant to both its Annual Incentive Program and its Share Incentive Plan. The Company amortizes the expense related to the shares awarded under the Share Incentive Plan and the premium awarded under the restricted share alternative of the Annual Incentive Program on a straight-line basis over the future vesting period (usually three to five years). Total expense recognized related to all restricted shares was $634 thousand and $559 thousand for the three months ended March 31, 2007 and 2006, respectively.

Table of Contents

Shares Issued to Trustees

The Company issues shares to Trustees for payment of their annual retainers. This expense is amortized by the Company on a straight-line basis over the year of service by the Trustees. Total expense recognized related to shares issued to Trustees was $40 thousand for both the three months ended March 31, 2007 and 2006.

Reclassifications

Certain reclassifications have been made to the prior period amounts to conform to the current period presentation.

3. Rental Properties

The following table summarizes the carrying amounts of rental properties as of March 31, 2007 and December 31, 2006 (in thousands):

	March 31, 2007	December 31, 2006
Buildings and improvements	$ 1,190,898	$ 1,189,676
Furniture, fixtures & equipment	8,206	8,147
Land	350,171	339,716
	1,549,275	1,537,539
Accumulated depreciation	(149,514)	(141,636)
Total	$ 1,399,761	$ 1,395,903

Depreciation expense on rental properties was $7.8 million and $7.0 million for the three months ended March 31, 2007 and 2006, respectively.

4. Unconsolidated Real Estate Joint Ventures

At March 31, 2007, the Company had a 20% investment interest in each of two unconsolidated real estate joint ventures, Atlantic-EPR I and Atlantic-EPR II. The Company accounts for its investment in these joint ventures under the equity method of accounting.

The Company recognized income of $120 and $112 (in thousands) from its investment in the Atlantic-EPR I joint venture during the first three months of 2007 and 2006, respectively. The Company also received distributions from Atlantic-EPR I of $136 and $129 (in thousands) during the first three months of 2007 and 2006, respectively.

Condensed financial information for Atlantic-EPR I is as follows as of and for the three months ended March 31, 2007 and 2006 (in thousands):

	2007	2006
Rental properties, net	$29,084	29,728
Cash	141	141
Long-term debt	16,057	16,387
Partners equity	13,063	13,375
Rental revenue	1,065	1,044
Net income	560	525

Table of Contents

The Company recognized income of $78 and $72 (in thousands) from its investment in the Atlantic-EPR II joint venture during the first three months of 2007 and 2006, respectively. The Company also received distributions from Atlantic-EPR II of $88 and $84 (in thousands) during the first three months of 2007 and 2006, respectively. Condensed financial information for Atlantic-EPR II is as follows as of and for the three months ended March 31, 2007 and 2006 (in thousands):

	2007	2006
Rental properties, net	$22,765	23,226
Cash	99	87
Long-term debt	13,803	14,080
Note payable to Entertainment Properties Trust	117	117
Partners equity	8,747	8,937
Rental revenue	694	694
Net income	336	319

The joint venture agreements for Atlantic-EPR I and Atlantic-EPR II allow the Company s partner, Atlantic of Hamburg, Germany (Atlantic), to exchange up to a maximum of 10% of its ownership interest per year in each of the joint ventures for common shares of the Company or, at the discretion of the Company, the cash value of those shares as defined in each of the joint venture agreements.

5. Share Incentive Plan

The Company maintains a Share Incentive Plan under which an aggregate of 3,000,000 common shares and options to purchase common shares, subject to adjustment in the event of certain capital events, may be granted. At March 31, 2007, there were 1,026,167 shares available for grant under the Share Incentive Plan.

Share Options

Share options granted under the Share Incentive Plan have exercise prices equal to the fair market value of a common share at the date of grant. The options may be granted for any reasonable term, not to exceed 10 years, and typically become exercisable at a rate of 20% per year over a five year period. For trustees, share options become exercisable over a one-year period. The Company generally issues new common shares upon option exercise. A summary of the Company s share option activity and related information is as follows:

	Number of Shares	Option Price Per Share	Weighted Average Exercise Price
Outstanding at December 31, 2006	981,673	$ 14.00 $43.75	$ 28.33
Exercised	(140,470)	16.05 43.75	29.41
Granted	86,945	60.03 65.50	64.88
Outstanding at March 31, 2007	928,148	14.00 65.50	31.59

The weighted average fair value of options granted was $7.91 and $5.03 during the three months ended March 31, 2007 and 2006, respectively. At March 31, 2007 and December 31, 2006, stock-option expense to be recognized in future periods was $1.2 million and $648 thousand, respectively. During the three months ended March 31, 2007, the intrinsic value of stock options exercised was $5.0 million.

Table of Contents

The following table summarizes outstanding options at March 31, 2007:

Exercise price range	Options outstanding	Weighted avg. life remaining	Weighted avg. exercise price	Aggregate intrinsic value (in thousands)
$14.00 19.99	196,372	3.4		