

HOME PROPERTIES INC  
Form 10-Q  
November 05, 2010

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

(Mark One)

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

**For the quarterly period ended SEPTEMBER 30, 2010**

**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: 1-13136  
HOME PROPERTIES, INC.**

(exact name of registrant as specified in its charter)

MARYLAND

16-1455126

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

850 Clinton Square, Rochester, New York

14604

(Address of principal executive offices)

(Zip Code)

(585) 546-4900

(Registrant's telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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  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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). 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 the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

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

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

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Common Stock  
\$.01 par value

Outstanding at October 31, 2010  
37,631,606

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PART I FINANCIAL INFORMATION  
ITEM 1. FINANCIAL STATEMENTS  
HOME PROPERTIES, INC.  
CONSOLIDATED BALANCE SHEETS  
SEPTEMBER 30, 2010 AND DECEMBER 31, 2009  
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)  
(UNAUDITED)

	2010	2009
<b>ASSETS</b>		
Real estate:		
Land	\$ 576,377	\$ 508,087
Construction in progress	160,303	184,617
Buildings, improvements and equipment	3,615,313	3,223,275
	4,351,993	3,915,979
Less: accumulated depreciation	(825,472)	(733,142)
Real estate, net	3,526,521	3,182,837
Cash and cash equivalents	7,881	8,809
Cash in escrows	34,837	27,278
Accounts receivable	12,131	14,137
Prepaid expenses	21,007	16,783
Deferred charges	13,518	13,931
Other assets	14,107	4,259
Total assets	\$ 3,630,002	\$ 3,268,034
<b>LIABILITIES AND EQUITY</b>		
Mortgage notes payable	\$ 2,324,958	\$ 2,112,645
Exchangeable senior notes	137,685	136,136
Line of credit	137,000	53,500
Accounts payable	21,507	19,695
Accrued interest payable	12,346	10,661
Accrued expenses and other liabilities	28,612	27,989
Security deposits	20,294	19,334
Total liabilities	2,682,402	2,379,960
Commitments and contingencies		
Equity:		
Common stock, \$0.01 par value; 80,000,000 shares authorized; 37,583,101 and 34,655,428 shares issued and outstanding at September 30, 2010 and December 31, 2009, respectively	376	347

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Excess stock, \$0.01 par value; 10,000,000 shares authorized; no shares issued or outstanding		
Additional paid-in capital	1,034,655	922,078
Distributions in excess of accumulated earnings	(311,743)	(261,313)
Total common stockholders equity	723,288	661,112
Noncontrolling interest	224,312	226,962
Total equity	947,600	888,074
Total liabilities and equity	\$ 3,630,002	\$ 3,268,034

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

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HOME PROPERTIES, INC.  
CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2010 AND 2009  
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)  
(UNAUDITED)

	2010	2009
Revenues:		
Rental income	\$ 120,067	\$ 115,611
Property other income	9,681	9,182
Interest income	10	4
Other income	1	29
Total revenues	129,759	124,826
Expenses:		
Operating and maintenance	51,361	51,302
General and administrative	5,553	6,101
Interest	31,098	30,773
Depreciation and amortization	32,350	29,932
Other expenses	2,213	
Total expenses	122,575	118,108
Income from continuing operations	7,184	6,718
Discontinued operations:		
Income from discontinued operations	18	524
Loss on disposition of property		(22)
Discontinued operations	18	502
Net income	7,202	7,220
Net income attributable to noncontrolling interest	(1,695)	(1,956)
Net income attributable to common stockholders	\$ 5,507	\$ 5,264
Basic earnings per share:		
Income from continuing operations	\$ 0.15	\$ 0.15
Discontinued operations		0.01
Net income attributable to common stockholders	\$ 0.15	\$ 0.16

Diluted earnings per share:



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Income from continuing operations	\$	0.15	\$	0.15
Discontinued operations				0.01
Net income attributable to common stockholders	\$	0.15	\$	0.16
Weighted average number of shares outstanding:				
Basic		37,357,579		32,972,794
Diluted		37,863,902		33,091,764
Dividends declared per share	\$	0.58	\$	0.67

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

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HOME PROPERTIES, INC.  
CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2010 AND 2009  
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)  
(UNAUDITED)

	2010	2009
Revenues:		
Rental income	\$ 351,006	\$ 347,111
Property other income	31,652	30,270
Interest income	21	18
Other income	78	397
Total revenues	382,757	377,796
Expenses:		
Operating and maintenance	159,050	158,702
General and administrative	18,221	18,238
Interest	91,459	91,583
Depreciation and amortization	93,709	89,433
Other expenses	2,836	
Total expenses	365,275	357,956
Income from continuing operations	17,482	19,840
Discontinued operations:		
Income (loss) from discontinued operations	23	(2,750)
Gain (loss) on disposition of property	(13)	13,471
Discontinued operations	10	10,721
Net income	17,492	30,561
Net income attributable to noncontrolling interest	(4,180)	(8,375)
Net income attributable to common stockholders	\$ 13,312	\$ 22,186
Basic earnings per share:		
Income from continuing operations	\$ 0.37	\$ 0.44
Discontinued operations		0.24
Net income attributable to common stockholders	\$ 0.37	\$ 0.68
Diluted earnings per share:		

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Income from continuing operations	\$	0.36	\$	0.44
Discontinued operations				0.23
Net income attributable to common stockholders	\$	0.36	\$	0.67
Weighted average number of shares outstanding:				
Basic		36,389,232		32,841,779
Diluted		36,830,743		32,905,711
Dividends declared per share	\$	1.74	\$	2.01

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

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HOME PROPERTIES, INC.  
CONSOLIDATED STATEMENTS OF EQUITY  
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2010 AND THE YEAR ENDED DECEMBER 31, 2009  
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)  
(UNAUDITED)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Distributions in Excess of Accumulated Earnings	Noncontrolling Interest	Totals
Balance, January 1, 2009	32,431,304	\$ 324	\$ 857,415	\$ (206,961)	\$ 260,754	\$ 911,532
Comprehensive income:						
Net income				34,419	12,659	47,078
Issuance of common stock, net	1,228,070	12	46,636			46,648
Stock-based compensation	6,746		7,291			7,291
Repurchase of common stock	(97,304)		(2,935)			(2,935)
Conversion of UPREIT Units for common stock	1,086,612	11	21,321		(21,332)	0
Adjustment of noncontrolling interest			(7,650)		7,650	0
Dividends and distributions paid				(88,771)	(32,769)	(121,540)
Balance, December 31, 2009	34,655,428	\$ 347	\$ 922,078	\$ (261,313)	\$ 226,962	\$ 888,074
Comprehensive income:						
Net income				13,312	4,180	17,492
Issuance of common stock, net	2,651,665	27	117,611			117,638
Stock-based compensation	6,206		6,073			6,073
Repurchase of common stock	(57,344)	(1)	(2,784)			(2,785)
Conversion of UPREIT Units for common stock	327,146	3	6,333		(6,336)	0
Issuance of UPREIT Units associated with property acquisition					4,845	4,845
Adjustment of noncontrolling interest			(14,656)		14,656	0
Dividends and distributions paid				(63,742)	(19,995)	(83,737)
Balance, September 30, 2010	37,583,101	\$ 376	\$ 1,034,655	\$ (311,743)	\$ 224,312	\$ 947,600

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

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HOME PROPERTIES, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2010 AND 2009  
(DOLLARS IN THOUSANDS)  
(UNAUDITED)

	2010	2009
Cash flows from operating activities:		
Net income	\$ 17,492	\$ 30,561
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	97,570	92,747
Amortization of debt discount	1,549	1,463
Loss (gain) on disposition of property	13	(13,471)
Stock-based compensation	6,073	5,890
Changes in assets and liabilities:		
Cash in escrows, net	(4,427)	1,418
Other assets	(10,649)	(981)
Accounts payable and accrued liabilities	2,595	(4,303)
Total adjustments	92,724	82,763
Net cash provided by operating activities	110,216	113,324
Cash flows from investing activities:		
Purchase of properties, net of mortgage notes assumed and UPREIT Units issued	(171,832)	
Additions to properties	(66,157)	(57,749)
Additions to construction in progress	(36,437)	(53,661)
Proceeds from (payments for) sale of properties, net	(13)	66,878
Purchase of notes receivable	(1,433)	
Additions to cash in escrows, net	(3,128)	(272)
Net cash used in investing activities	(279,000)	(44,804)
Cash flows from financing activities:		
Proceeds from sale of common stock, net	117,638	2,236
Repurchase of common stock	(2,785)	(2,249)
Proceeds from mortgage notes payable	220,704	115,493
Payments of mortgage notes payable	(164,029)	(88,665)
Proceeds from line of credit	342,000	362,000
Payments on line of credit	(258,500)	(361,500)
Payments of deferred loan costs, net	(3,432)	(4,390)
Additions to cash in escrows, net	(3)	(9)
Dividends and distributions paid	(83,737)	(91,124)
Net cash provided by (used in) financing activities	167,856	(68,208)

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Net increase (decrease) in cash and cash equivalents	(928)	312
Cash and cash equivalents:		
Beginning of year	8,809	6,567
End of period	\$ 7,881	\$ 6,879

Supplemental disclosure of non-cash investing and financing activities:

Mortgage loans assumed with property acquisitions	\$ 155,638	\$
Issuance of UPREIT Units associated with property acquisition	4,845	
Exchange of UPREIT Units for common stock	6,336	18,279
Transfers of construction in progress to buildings, improvements and equipment	60,827	
Additions to properties included in accounts payable	4,302	2,181
Mortgage note premium write-off		615

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

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HOME PROPERTIES, INC.  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
(DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)  
(UNAUDITED)

**1. Unaudited Interim Financial Statements**

The interim consolidated financial statements of Home Properties, Inc. (the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and the applicable rules and regulations of the Securities and Exchange Commission (SEC). Accordingly, certain disclosures that would accompany annual financial statements prepared in accordance with GAAP are omitted. The year-end balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP. In the opinion of management, all adjustments, consisting solely of normal recurring adjustments, necessary for the fair statement of the consolidated financial statements for the interim periods have been included. The current period's results of operations are not necessarily indicative of results which ultimately may be achieved for the year. The interim consolidated financial statements and notes thereto should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Form 10-K for the year ended December 31, 2009.

**2. Organization and Basis of Presentation**

*Organization*

The Company was formed in November 1993, as a Maryland corporation and is engaged in the ownership, management, acquisition, rehabilitation and development of residential apartment communities primarily in selected Northeast and Mid-Atlantic regions of the United States. The Company conducts its business through Home Properties, L.P. (the Operating Partnership), a New York limited partnership. As of September 30, 2010, the Company operated 116 apartment communities with 39,609 apartments. Of this total, the Company owned 115 communities, consisting of 38,741 apartments, and managed as general partner, one partnership that owned 868 apartments.

The Company elected to be taxed as a Real Estate Investment Trust (REIT) under the Internal Revenue Code, as amended, for all periods presented. A corporate REIT is a legal entity which holds real estate interests and must meet a number of organizational and operational requirements, including a requirement that it currently distribute at least 90% of its adjusted taxable income to stockholders. As a REIT, the Company generally will not be subject to corporate level tax on taxable income it distributes currently to its stockholders. The Company distributed in excess of 100% of its taxable income for the periods presented. Therefore, no provision has been made for federal income taxes.

*Basis of Presentation*

The accompanying consolidated financial statements include the accounts of the Company and its ownership of 76.6% of the limited partnership units in the Operating Partnership (UPREIT Units) at September 30, 2010 (74.7% at December 31, 2009). The remaining 23.4% is included as noncontrolling interest in these consolidated financial statements at September 30, 2010 (25.3% at December 31, 2009). The Company owns a 1.0% general partner interest in the Operating Partnership and the remainder indirectly as a limited partner through its wholly owned subsidiary, Home Properties I, LLC, which owns 100% of Home Properties Trust, which is the limited partner. Home Properties Trust was formed in September 1997, as a Maryland real estate trust and as a qualified REIT subsidiary (QRS) and owns the Company's share of the limited partner interests in the Operating Partnership.

The accompanying consolidated financial statements include the accounts of Home Properties Resident Services, Inc. (HPRS or the Management Company). The Management Company is a wholly owned subsidiary of the Company. In addition, the Company consolidates one affordable housing limited partnership in accordance with Financial Accounting Standards Board (FASB) authoritative guidance for the consolidation of variable interest entities. All significant inter-company balances and transactions have been eliminated in these consolidated financial statements.

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**3. Recently Adopted Accounting Standards**

Effective January 1, 2010, the Company adopted the amended guidance related to the consolidation of variable interest entities (Accounting Standards Update 2009-17, *Consolidations (Topic 810): Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities*). The Company's adoption of this authoritative guidance did not have any impact on its financial position and results of operations.

**4. Earnings Per Common Share**

Basic earnings per share (EPS) is computed as net income attributable to common stockholders divided by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issuable through stock-based compensation including stock options (using the treasury stock method) and the conversion of any exchangeable senior notes. The exchange of an UPREIT Unit for common stock will have no effect on diluted EPS as unitholders and common stockholders effectively share equally in the net income of the Operating Partnership. Income from continuing operations and discontinued operations is the same for both the basic and diluted calculation.

The reconciliation of the basic and diluted earnings per share for the three and nine months ended September 30, 2010 and 2009 follows:

	Three Months		Nine Months	
	2010	2009	2010	2009
<b>Numerator:</b>				
Income from continuing operations	\$ 7,184	\$ 6,718	\$ 17,482	\$ 19,840
Less: Income from continuing operations attributable to noncontrolling interest	(1,691)	(1,820)	(4,179)	(5,420)
Income from continuing operations attributable to common stockholders	\$ 5,493	\$ 4,898	\$ 13,303	\$ 14,420
Discontinued operations	\$ 18	\$ 502	\$ 10	\$ 10,721
Less: Discontinued operations attributable to noncontrolling interest	(4)	(136)	(1)	(2,955)
Discontinued operations attributable to common stockholders	\$ 14	\$ 366	\$ 9	\$ 7,766
<b>Denominator:</b>				
Basic weighted average number of common shares outstanding	37,357,579	32,972,794	36,389,232	32,841,779
Effect of dilutive stock options	422,757	79,439	387,500	45,632
Effect of phantom and restricted shares	83,566	39,531	54,011	18,300
Diluted weighted average number of common shares outstanding	37,863,902	33,091,764	36,830,743	32,905,711

**Earnings per common share:**



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Basic earnings per share:								
Income from continuing operations	\$	0.15	\$	0.15	\$	0.37	\$	0.44
Discontinued operations				0.01				0.24
Net income attributable to common stockholders	\$	0.15	\$	0.16	\$	0.37	\$	0.68
Diluted earnings per share:								
Income from continuing operations	\$	0.15	\$	0.15	\$	0.36	\$	0.44
Discontinued operations				0.01				0.23
Net income attributable to common stockholders	\$	0.15	\$	0.16	\$	0.36	\$	0.67

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**4. Earnings Per Common Share (continued)**

Unexercised stock options to purchase 1,753,345 and 2,147,816 shares of the Company's common stock for the three months ended September 30, 2010 and 2009, respectively, and 1,753,345 and 3,119,409 shares of the Company's common stock for the nine months ended September 30, 2010 and 2009, respectively, were not included in the computations of diluted EPS because the effects would be antidilutive. Also, in conjunction with the issuance of the Senior Notes (as defined in Note 7), there were 331,257 and 332,721 potential shares issuable under certain circumstances, of which all are considered antidilutive as of September 30, 2010 and 2009, respectively.

**5. Variable Interest Entities**

The Company is the general partner in one variable interest entity ( VIE ) syndicated using low income housing tax credits under Section 42 of the Internal Revenue Code. As general partner, the Company manages the day-to-day operations of the partnership for a management fee. In addition, the Company has an operating deficit guarantee and tax credit guarantee to the limited partners of that partnership (as discussed in Note 15). The Company is responsible for funding operating deficits to the extent there are any and can receive operating incentive awards when cash flows reach certain levels. Included in the Consolidated Balance Sheet for the VIE as of September 30, 2010 are total assets of \$9,899, total liabilities of \$16,562 and partners' deficit of \$6,663, respectively. Of the \$16,562 in total liabilities, \$15,762 represents non-recourse mortgage debt. As more fully described in Note 16, the Company's general partnership interest in the VIE was sold on October 13, 2010.

**6. Acquisitions***Acquisitions of Real Estate*

On April 1, 2010, the Company acquired two communities located in Westminster, Maryland from the same seller. Middlebrooke Apartments and Westbrooke Apartments, with 208 units and 110 units, respectively, were purchased for \$17,350 and \$6,350, respectively. In connection with these acquisitions, closing costs of \$248 were incurred and are included in other expenses.

On June 17, 2010, the Company acquired Annapolis Roads Apartments in Annapolis, Maryland, a property it had managed for the prior owner since 2000. The total purchase price for the 282 unit property of \$32,500 included the assumption of an existing \$20,043 fixed rate mortgage at an interest rate of 5.95% maturing in January 2011 (fair market value of \$20,238), \$4,845 in 98,728 UPREIT Units and the balance paid in cash. Closing costs of \$357 were incurred and included in other expenses.

On July 29, 2010, the Company acquired The Greens at Columbia, a 168 unit community in Columbia, Maryland for a total purchase price of \$25,600. Consideration for the purchase included the assumption of an existing \$9,596 fixed-rate mortgage at an interest rate of 4.93%, maturing in August 2014 (fair market value of \$9,947). Debt assumption costs of \$112 were capitalized and will be amortized over the remaining term of the debt. In connection with this acquisition, closing costs of \$302 were incurred and are included in other expenses.

On August 5, 2010, the Company acquired Village at Potomac Falls, a 247 unit apartment community located in Sterling, Virginia, for a total cash purchase price of \$38,500. In connection with this acquisition, closing costs of \$177 were incurred and are included in other expenses.

On September 30, 2010, the Company acquired Charleston Place, an 858 unit apartment community located in Ellicott City, Maryland for a total purchase price of \$103,000. Consideration for the purchase included the assumption of existing debt totaling \$70,750 at fixed-rates with a weighted average interest rate of 5.31%, maturing in September 2015 (fair market value of \$75,702), with the remainder paid in cash. Debt assumption costs of \$728 were capitalized and will be amortized over the remaining term of the debt. Acquisition closing costs of \$1,159 were incurred and are included in other expenses.



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**6. Acquisitions (continued)**

On September 30, 2010, the Company acquired The Courts at Fair Oaks, a 364 unit apartment community located in Fairfax, Virginia for a total purchase price of \$70,100. Consideration for the purchase included the assumption of an existing \$46,000 fixed-rate mortgage at an interest rate of 5.66%, maturing in August 2019 (fair market value of \$49,751), with the remainder paid in cash. Debt assumption costs of \$472 were capitalized and will be amortized over the remaining term of the debt. Acquisition closing costs of \$301 were incurred and are included in other expenses.

On September 30, 2010, the Company acquired Crescent Club, a 257 unit apartment community located in Suffolk County, Long Island, New York for a total cash purchase price of \$31,250. Acquisition closing costs of \$260 were incurred and are included in other expenses.

The following unaudited pro forma information was prepared as if the 2010 transactions related to the acquisition of apartment communities occurred as of January 1, 2009. The pro forma financial information is based upon the historical consolidated financial statements and is not necessarily indicative of the consolidated results which actually would have occurred if the transactions had been consummated at January 1, 2009, nor does it purport to represent the results of operations for future periods. Adjustments to the pro forma financial information for the nine months ended September 30, 2010 and 2009 consist principally of providing net operating activity and recording interest, depreciation and amortization from January 1, 2009 to the acquisition date as appropriate.

	Nine Months	
	2010	2009
Pro forma total revenues	\$ 403,548	\$ 402,088
Pro forma net income attributable to common shareholders	\$ 14,540	\$ 23,155
Pro forma earnings per common share:		
Basic	\$ 0.40	\$ 0.71
Diluted	\$ 0.39	\$ 0.70

Included in the consolidated statements of income for the nine months ended September 30, 2010 are total revenues of \$3,674 and net income attributable to common shareholders of \$547 since the respective date of acquisition through September 30, 2010 for the 2010 acquired apartment communities.

All of the 2010 acquired apartment communities were recorded at fair value which approximated actual purchase price. None of the 2010 acquisitions were subject to bargain purchase options or resulted in goodwill being recorded.

*Acquisition of Notes Receivable*

On September 22, 2010, the Company purchased two non-performing mortgage notes from a community bank for \$1,433 in an arm s length transaction. Both notes are in default. One of the notes, purchased for \$1,015, is secured by land and buildings, and is operated as a strip center adjacent to one of our apartment communities. The other note, purchased for \$418 is secured by vacant land. The notes were purchased at face value including accrued interest and late fees. The Company has notified the existing tenants at the strip center that it has exercised rights to receive rents under the terms of the mortgage agreements. Rents in the amount of approximately \$20 per month will be used to pay taxes and public utilities and to relieve indebtedness secured by the mortgage. In accordance with authoritative guidance, we recognize impairment to the extent the fair value of the collateral is less than the carrying amount of our investment in the notes receivable. Interest income, if any, will be recognized on the cost recovery method. As of September 30, 2010, there was no impairment recognized and no interest income recorded. Notes receivable of \$1,433 are included in other assets on the Consolidated Balance Sheet as of September 30, 2010.

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**7. Development**

During the second quarter of 2010, construction activities on a project in Silver Spring, Maryland, 1200 East West Highway, a 14-story high rise with 247 apartment units, neared completion and the project experienced initial occupancy. By the end of the third quarter of 2010, there were 189 units rented and occupied. The construction in progress for this development was \$40,477 as of September 30, 2010.

During the second quarter of 2010, construction activities neared completion on the first phase (two buildings with 202 units) of a project in Alexandria, Virginia, the Courts at Huntington Station. By the end of the third quarter of 2010, there were 115 units rented and occupied. Construction on the second phase (two buildings with 219 units) has commenced and construction is scheduled to be completed in the second quarter of 2011. The construction in progress for this development was \$84,717 as of September 30, 2010.

The Company also has two projects in pre-construction development: Cobblestone Square located in Fredericksburg, Virginia, consisting of approximately 314 apartment units; and Ripley Street located in Silver Spring, Maryland, an 18-story high rise with approximately 379 apartment units. Both projects are on entitled land that the Company purchased from other developers and both are in the final stages of the design process. The construction in progress for these developments was \$35,109 as of September 30, 2010.

**8. Exchangeable Senior Notes**

In October 2006, the Company issued \$200,000 of exchangeable senior notes under an Indenture Agreement (the Indenture), with a coupon rate of 4.125% (Senior Notes). In the fourth quarter of 2008, the Company repurchased \$60,000 principal amount of the Senior Notes, leaving \$140,000 outstanding. The Senior Notes are exchangeable into cash equal to the principal amount of the notes and, at the Company's option, cash or common stock for the exchange value, to the extent that the market price of common stock exceeds the initial exchange price of \$73.34 per share, subject to adjustment. The exchange price is adjusted for payments of dividends in excess of the reference dividend per the Indenture of \$0.64 per share. The notes are not redeemable at the option of the Company for five years, except to preserve the status of the Company as a REIT. Holders of the notes may require the Company to repurchase the notes upon the occurrence of certain designated events. In addition, prior to November 1, 2026, the holders may require the Company to repurchase the notes on November 1, 2011, 2016 and 2021. The notes will mature on November 1, 2026, unless previously redeemed, repurchased or exchanged in accordance with their terms prior to that date. The notes are structurally subordinated to the secured indebtedness of the Company. The Company is not subject to any financial covenants under the Indenture. In addition, the Indenture will not restrict the ability to pay distributions, incur debt or issue or repurchase securities.

The following table provides information about the Senior Notes as of September 30, 2010 and December 31, 2009:

	2010	2009
Principal amount of liability component	\$ 140,000	\$ 140,000
Unamortized discount	(2,315)	(3,864)
Carrying amount of liability component	\$ 137,685	\$ 136,136
Carrying amount of equity component	\$ 13,950	\$ 13,950

The following table provides information about the Senior Notes for the three and nine months ended September 30, 2010 and 2009:

Three Months		Nine Months	
2010	2009	2010	2009

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Coupon interest	\$	1,444	\$	1,444	\$	4,331	\$	4,331
Issuance cost amortization		137		137		410		410
Discount amortization		523		494		1,549		1,464
Total interest expense	\$	2,104	\$	2,075	\$	6,290	\$	6,205
Effective interest rate		5.75%		5.75%		5.75%		5.75%
Conversion price per share, as adjusted	\$	72.87	\$	72.92	\$	72.87	\$	72.92

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**9. Line of Credit**

As of September 30, 2010, the Company had a \$175,000 unsecured line of credit agreement which expires August 31, 2011, with an optional one-year extension. The Company had \$137,000 outstanding under the credit facility on September 30, 2010. Borrowings under the line of credit bear interest at rates ranging from 2.50% to 3.25% over the one-month LIBOR rate, increasing at higher levels of outstanding indebtedness, with a LIBOR floor of 1.50%. The one-month LIBOR was 0.26% at September 30, 2010, resulting in an effective rate of 4.50% for the Company.

The credit agreement relating to this line of credit requires the Company to maintain certain financial covenants. The Company was in compliance with these financial covenants for the nine months ended September 30, 2010.

The Company's line of credit agreement provides the ability to issue up to \$20,000 in letters of credit. While the issuance of letters of credit does not increase borrowings outstanding under the line of credit, it does reduce the amount available. At September 30, 2010, the Company had outstanding letters of credit of \$4,379 and the amount available on the credit facility was \$33,621.

**10. Fair Value of Financial Instruments**

The Company follows the authoritative guidance for fair value measurements ( ASC 820-10 ), when valuing its financial instruments for disclosure purposes. The valuation of financial instruments requires the Company to make estimates and judgments that affect the fair value of the instruments. The Company determined the fair value of its mortgage notes payable and line of credit facility using a discounted future cash flow technique that incorporates a market interest yield curve with adjustments for duration, loan to value, and risk profile (level 2 inputs, as defined by ASC 820-10). In determining the market interest yield curve, the Company considered its BBB credit rating. The Company based the fair value of its Senior Notes using quoted prices (a level 1 input, as defined by ASC 820-10).

At September 30, 2010 and December 31, 2009, the fair value of the Company's total debt, including the Senior Notes and line of credit, amounted to a liability of \$2,769,130 and \$2,337,866, respectively, compared to its carrying amount of \$2,599,643 and \$2,302,281, respectively.

**11. Interest Capitalized**

Capitalized interest associated with communities under development or rehabilitation totaled \$2,061 and \$2,336 for the three months ended September 30, 2010 and 2009, respectively; \$7,622 and \$6,206 for the nine months ended September 30, 2010 and 2009, respectively.

**12. Stockholders Equity***At-the-Market Equity Offering Programs*

On December 3, 2009, the Company initiated an At-the-Market ( ATM ) equity offering program through which it was authorized to sell up to 3.7 million shares of common stock (not to exceed \$150,000 of gross proceeds), from time to time in ATM offerings or negotiated transactions. The following are issuances of common stock of this program since inception through the completion of the program on May 11, 2010:

Period	Number of Shares Sold	Gross Proceeds	Net Proceeds	Average Sales Price
Fourth quarter 2009	871,600	\$ 39,830	\$ 38,916	\$ 45.70
First quarter 2010	1,285,700	60,092	58,856	46.74
Second quarter 2010	1,021,400	50,078	49,273	49.03
Total	3,178,700	\$ 150,000	\$ 147,045	\$ 47.19





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**12. Stockholders Equity (continued)**

On September 17, 2010, the Company registered another ATM equity offering program through which it is authorized to sell up to 3.6 million common shares of common stock, from time to time in ATM offerings or negotiated transactions. There were no shares issued from this program since inception through September 30, 2010.

*Dividends and Distributions*

On August 26, 2010, the Company paid a dividend in the amount of \$0.58 per share of common stock to stockholders and a distribution of \$0.58 per UPREIT Unit to unitholders of record as of the close of business on August 16, 2010.

**13. Segment Reporting**

The Company is engaged in the ownership and management of market rate apartment communities. Each apartment community is considered a separate operating segment. Each segment on a stand alone basis is less than 10% of the revenues, net operating income, and assets of the combined reported operating segment and meets all of the aggregation criteria under authoritative guidance. The operating segments are aggregated as Core and Non-core properties.

Non-segment revenue to reconcile to total revenue consists of interest income and other income. Non-segment assets to reconcile to total assets include cash and cash equivalents, cash in escrows, accounts receivable, prepaid expenses, deferred charges and other assets.

Core properties consist of all apartment communities which have been owned more than one full calendar year. Therefore, the Core properties represent communities owned as of January 1, 2009. Non-core properties consist of the VIE and apartment communities acquired or developed during 2009 and 2010, such that full year comparable operating results are not available.

The Company assesses and measures segment operating results based on a performance measure referred to as net operating income. Net operating income is defined as total revenues less operating and maintenance expenses. The accounting policies of the segments are the same as those described in Notes 1, 2 and 3 of the Company's Form 10-K for the year ended December 31, 2009.

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**13. Segment Reporting (continued)**

The revenues and net operating income for each of the operating segments are summarized for the three and nine months ended September 30, 2010 and 2009 as follows:

	Three Months		Nine Months	
	2010	2009	2010	2009
Revenues:				
Apartments owned				
Core properties	\$ 124,350	\$ 123,633	\$ 373,733	\$ 373,909
Non-core properties	5,398	1,160	8,925	3,472
Reconciling items	11	33	99	415
<b>Total revenues</b>	<b>\$ 129,759</b>	<b>\$ 124,826</b>	<b>\$ 382,757</b>	<b>\$ 377,796</b>
Net operating income:				
Apartments owned				
Core properties	\$ 75,811	\$ 73,287	\$ 220,417	\$ 218,147
Non-core properties	2,576	204	3,191	532
Reconciling items	11	33	99	415
Net operating income, including reconciling items	78,398	73,524	223,707	219,094
General and administrative expenses	(5,553)	(6,101)	(18,221)	(18,238)
Interest expense	(31,098)	(30,773)	(91,459)	(91,583)
Depreciation and amortization	(32,350)	(29,932)	(93,709)	(89,433)
Other expenses	(2,213)		(2,836)	
<b>Income from continuing operations</b>	<b>\$ 7,184</b>	<b>\$ 6,718</b>	<b>\$ 17,482</b>	<b>\$ 19,840</b>

The assets for each of the reportable segments are summarized as follows as of September 30, 2010 and December 31, 2009:

	2010	2009
Assets:		
Apartments owned		
Core properties	\$ 2,951,658	\$ 2,975,642
Non-core properties	574,863	207,195
Reconciling items	103,481	85,197
<b>Total assets</b>	<b>\$ 3,630,002</b>	<b>\$ 3,268,034</b>

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**14. Disposition of Property and Discontinued Operations**

The Company reports its property dispositions as discontinued operations as prescribed by the authoritative guidance. Pursuant to the definition of a component of an entity, assuming no significant continuing involvement by the former owner after the sale, the sale of an apartment community is considered a discontinued operation. In addition, apartment communities classified as held for sale are also considered discontinued operations. The Company generally considers assets to be held for sale when all significant contingencies surrounding the closing have been resolved, which often corresponds with the actual closing date.

Included in discontinued operations for the three and nine months ended September 30, 2009 are the operating results of five apartment communities sold in three separate transactions during 2009 (the 2009 Disposed Communities ). Included in discontinued operations for the three and nine months ended September 30, 2010 are the operating results of the wind-up activities for the 2009 Disposed Communities. For purposes of the discontinued operations presentation, the Company only includes interest expense and losses from early extinguishment of debt associated with specific mortgage indebtedness of the properties that are sold or held for sale.

The operating results of discontinued operations are summarized for the three and nine months ended September 30, 2010 and 2009 as follows:

	Three Months		Nine Months	
	2010	2009	2010	2009
Revenues:				
Rental income	\$ 9	\$ 1,395	\$ 23	\$ 4,926
Property other income	9	114	30	492
Total revenues	18	1,509	53	5,418
Expenses:				
Operating and maintenance		597	30	2,494
Interest expense, including prepayment penalties				4,497
Depreciation and amortization		388		1,177
Total expenses		985	30	8,168
Income (loss) from discontinued operations	\$ 18	\$ 524	\$ 23	\$ (2,750)

**15. Commitments and Contingencies***Letters of Credit*

As of September 30, 2010, the Company had issued \$4,379 in letters of credit, which were provided under the Company's \$175,000 unsecured line of credit agreement. The letters of credit were required to be issued under certain tax escrow agreements, workers compensation and health insurance policies, and construction projects.

*Debt Covenants*

The line of credit agreement contains restrictions which, among other things, require maintenance of certain financial ratios.

Included in the Company's consolidated balance sheet at September 30, 2010 are assets of Home Properties Fair Oaks, LLC, owner of the Courts at Fair Oaks, Fairfax County, VA, that are pledged as collateral for specific indebtedness and are not available to satisfy any other obligations of the Company.



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**15. Commitments and Contingencies (continued)**

*Tax Protection Obligations*

In connection with various UPREIT transactions, the Company has agreed to maintain certain levels of nonrecourse debt for a period of 5 to 10 years associated with the contributed properties acquired. In addition, the Company is restricted in its ability to sell certain contributed properties (17% by number of apartment communities of the owned portfolio) for a period of 7 to 15 years except through a tax deferred like-kind exchange. The remaining terms on the sale restrictions range from 3 months to 7 years.

*Limited Partnership*

For periods before October 13, 2010, the Company, through its general partnership interest in an affordable property limited partnership, had guaranteed certain low income housing tax credits to limited partners for a period after September 30, 2010 of six years totaling approximately \$3,000. As of September 30, 2010, there were no known conditions that would make such payments necessary relating to these guarantees. In addition, the Company, acting as general partner in this partnership, was obligated to advance funds to meet partnership operating deficits. As more fully described in Note 16, the Company's general partner interest in this entity was sold on October 13, 2010, relieving the Company of the operating deficit guarantee to the limited partners of that partnership.

*Contingencies*

The Company is not a party to any legal proceedings which are expected to have a material adverse effect on the Company's liquidity, financial position or results of operations. The Company is subject to a variety of legal actions for personal injury or property damage arising in the ordinary course of its business, most of which are covered by liability insurance. Various claims of employment and resident discrimination are also periodically brought, most of which also are covered by insurance. While the resolution of these matters cannot be predicted with certainty, management believes that the final outcome of such legal proceedings and claims will not have a material adverse effect on the Company's liquidity, financial position or results of operations.

**16. Subsequent Events**

On October 26, 2010, the Board of Directors declared a dividend of \$0.58 per share on the Company's common stock and approved a distribution of \$0.58 per UPREIT Unit for the quarter ended September 30, 2010. This is the equivalent of an annual distribution of \$2.32 per share/unit. The dividend and distribution is payable November 23, 2010, to stockholders and unitholders of record on November 12, 2010.

On October 13, 2010, the Company sold its general partnership interest in an 868 unit affordable limited partnership, which is consolidated as a VIE (as more fully described in Note 5) for all periods presented. The sale price included the assumption by the buyer of the existing mortgage debt of \$15,762 and \$50 cash. In connection with this transaction, the Company will realize a gain of approximately \$500 during the fourth quarter of 2010. Per authoritative guidance, held for sale treatment is not applied until all contingencies under the contract have been mitigated. Due to the nature of this transaction and the limited number of buyers able to complete the sale as of September 30, 2010, significant financing contingencies existed which would have prevented the close of this sale until these contingencies were successfully mitigated. These contingencies were successfully mitigated on October 13, 2010. Giving consideration to the facts and circumstances, the Company will classify the results of the VIE as discontinued operations in the fourth quarter of 2010.

On October 18, 2010, the Company acquired a 120 unit apartment community located in Aurora, Illinois, a suburb of Chicago, for a total purchase price of \$14,475. In connection with this acquisition, closing costs of approximately \$60 were incurred and will be included in other expenses for the fourth quarter of 2010.

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HOME PROPERTIES, INC.  
ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS  
OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION  
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The following discussion should be read in conjunction with the accompanying consolidated financial statements and notes thereto.

**Forward-Looking Statements**

This discussion contains forward-looking statements. Historical results and percentage relationships set forth in the consolidated financial statements, including trends which might appear, should not be taken as indicative of future operations. The Company considers portions of the information to be forward-looking statements within the meaning of Section 27A of the Securities Exchange Act of 1933 and Section 21E of the Securities Exchange Act of 1934, both as amended, with respect to the Company's expectations for future periods. Some examples of forward-looking statements include statements related to acquisitions (including any related pro forma financial information), future capital expenditures, potential development and redevelopment opportunities, projected costs and rental rates for development and redevelopment projects, financing sources and availability, and the effects of environmental and other regulations. Although the Company believes that the expectations reflected in those forward-looking statements are based upon reasonable assumptions, it can give no assurance that its expectations will be achieved. Factors that may cause actual results to differ include general economic and local real estate conditions, the weather and other conditions that might affect operating expenses, the timely completion of repositioning activities and development within anticipated budgets, the actual pace of future development, acquisitions and sales, and continued access to capital to fund growth. For this purpose, any statements contained in this Form 10-Q that are not statements of historical fact should be considered to be forward-looking statements. Some of the words used to identify forward-looking statements include believes, anticipates, plans, expects, seeks, estimates, and any other expressions. Readers should exercise caution in interpreting and relying on forward-looking statements since they involve known and unknown risks, uncertainties and other factors which are, in some cases, beyond the Company's control and could materially affect the Company's actual results, performance or achievements.

**Liquidity and Capital Resources**

*General*

In 2000, the Company obtained an investment grade rating from Fitch, Inc. The rating in effect at September 30, 2010 (no change from initial rating) is a corporate credit rating of BBB (Triple B).

The Company's principal liquidity demands are expected to be distributions to the common stockholders and holders of UPREIT Units, capital improvements and repairs and maintenance for its properties, acquisition and development of additional properties and debt repayments. The Company may also acquire equity ownership in other public or private companies that own and manage portfolios of apartment communities.

The Company intends to meet its short-term liquidity requirements through net cash flows provided by operating activities and its existing bank line of credit, described below. The Company considers its ability to generate cash to be adequate to meet all operating requirements, including availability to pay dividends to its stockholders and make distributions to its unitholders in accordance with the provisions of the Internal Revenue Code, as amended, applicable to REITs.

*Cash Flow Summary*

The Company's net cash flow from operating activities was \$110 million in 2010 and \$113 million in 2009. The \$3 million decrease was primarily due to increased usage of cash for rate-lock deposits on mortgage financings of \$6 million included in other assets and \$5 million higher funding of escrows included in cash held in escrows, partially offset by timing differences in cash disbursements between periods which generated \$7 million higher cash flow.

**Table of Contents****Liquidity and Capital Resources (continued)**

Cash used in investing activities was \$279 million during 2010 compared to \$45 million in 2009. The \$234 million increase in investing between periods is primarily due to the \$172 million used for acquisition communities in 2010 as compared to no acquisitions in 2009. The 2009 period received the benefit of \$67 million proceeds from the sale of properties, while the 2010 period realized no property sales. Cash outflows for capital improvements were \$66 million in 2010 compared to \$58 million in 2009. The consistent outflow in both periods reflects management's strategy to continually reposition and perform selective rehabilitation in markets that are able to support rent increases. Cash outflows for additions to construction in progress were \$36 million in 2010 as compared to \$54 million in 2009. The lower spending on development in 2010 reflects the completion of one major project during 2010 compared to the active construction of two communities in 2009.

Net cash provided by financing activities totaled \$168 million in 2010. Cash flows from the sale of common stock under the ATM offering of \$108 million, net borrowing under our line of credit of \$84 million, net proceeds from mortgage financing of \$57 million and proceeds from stock option exercises of \$8 million and were partially offset by distributions paid to stockholders and UPREIT Unitholders of \$84 million. Net cash used in financing activities totaled \$68 million for 2009, primarily as a result of net proceeds from mortgage financing of \$27 million being more than offset by distributions paid to stockholders and UPREIT Unitholders of \$91 million.

***Line of Credit***

As of September 30, 2010, the Company had a \$175 million unsecured line of credit agreement with M&T Bank, as administrative agent and lead bank, which expires August 31, 2011, with an optional one-year extension. The Company had \$137 million outstanding under the credit facility on September 30, 2010. The line of credit agreement provides the ability to issue up to \$20 million in letters of credit. While the issuance of letters of credit does not increase the borrowings outstanding under the line of credit, it does reduce the amount available. At September 30, 2010, the Company had outstanding letters of credit of \$4.4 million and the amount available on the credit facility was \$33.6 million.

Borrowings under the line of credit bear interest at rates ranging from 2.50% to 3.25% over the one-month LIBOR rate, increasing at higher levels of outstanding indebtedness, with a LIBOR floor of 1.50%. The one-month LIBOR was 0.26% at September 30, 2010, resulting in an effective rate of 4.50% for the Company. Accordingly, increases in the one-month LIBOR above 1.50% will increase the Company's interest expense and as a result will affect the Company's results of operations and financial condition.

***Exchangeable Senior Notes***

In October 2006, the Company issued \$200 million of exchangeable senior notes with a coupon rate of 4.125% (Senior Notes), which generated net proceeds of \$195.8 million. The net proceeds were used to repurchase 933,000 shares of common stock for a total of \$58 million, pay down \$70 million on the line of credit, with the balance used for redemption of the Series F Preferred Shares and property acquisitions. During the fourth quarter of 2008, the Company repurchased \$60 million of the Senior Notes for \$45.4 million. The exchange terms and conditions are more fully described under Contractual Obligations and Other Commitments, below.

***Indebtedness***

As of September 30, 2010, the weighted average interest rate on the Company's total indebtedness of \$2.6 billion was 5.30% with staggered maturities averaging approximately six years. Approximately 86% of total indebtedness is at fixed rates. This limits the exposure to changes in interest rates, minimizing the effect of interest rate fluctuations on the Company's results of operations and cash flows.

As of September 30, 2010, the Company has refinanced \$125 million of the \$146 million in debt maturing in 2010, leaving only one loan of \$21 million maturing within 2010. Application has been made to a Government Sponsored Entity (GSE) for refinance. In addition, \$184 million of the \$298 million in mortgage debt that matures in 2011 was refinanced on October 29, 2010. The Company is currently in discussions with the GSEs relative to other maturing transactions and will continue to take advantage of its relationships with the GSEs and the low interest rate environment to further its refinancing of existing debt obligations.





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**Liquidity and Capital Resources (continued)**

*Unencumbered Assets*

The Company increased the percentage of unencumbered assets of the total property pool from 20% at the end of 2009, to 21% as of September 30, 2010. Higher levels of unsecured assets add borrowing flexibility because more capacity is available for unsecured debt under the terms of the Company's unsecured line of credit agreement.

*UPREIT Units*

The Company believes that the issuance of UPREIT Units for property acquisitions will continue to be a potential source of capital for the Company. During the first nine months of 2010, the Company issued \$4.8 million in 98,728 UPREIT Units as consideration for one acquired property.

*Property Dispositions*

During 2009, the Company sold five communities, with a total of 1,333 units, for \$108.3 million. A gain on sale of approximately \$24.3 million was realized from these sales.

Management has not specifically targeted additional communities for sale in 2010.

*Universal Shelf Registration*

On March 3, 2010, the Company filed a Form S-3 universal shelf registration statement with the SEC that registers the issuance, from time to time, of common stock, preferred stock or debt securities. The Company may offer and sell securities issued pursuant to the universal shelf registration statement after a prospectus supplement, describing the type of security and amount being offered, is filed with the SEC. Sales of common stock under the Company's ATM offering in the six months from December 2009 to May 2010 described below were made under this registration statement.

*At-the-Market Equity Offering Program*

On December 3, 2009, the Company initiated an At-the-Market ( ATM ) equity offering program through which it was authorized to sell up to 3.7 million shares of common stock (not to exceed \$150 million of gross proceeds), from time to time in ATM offerings or negotiated transactions. From December 2009 through completion of the offering in May 2010, the Company issued 3,178,700 shares of common stock at an average price per share of \$47.19, for aggregate gross proceeds of \$150.0 million and aggregate net proceeds of \$147.0 million after deducting commissions and other transaction costs of approximately \$3.0 million.

On September 17, 2010, the Company filed a prospectus supplement with respect to another ATM equity offering program, with similar terms and conditions as the December 2009 program, through which it is authorized to sell up to 3,600,000 common shares of common stock, from time to time in ATM offerings or negotiated transactions. There were no shares issued from this program since inception through September 30, 2010. If shares are issued, the Company intends to use the net proceeds from the offering for general corporate purposes, which may include the repayment of debt, working capital, capital expenditures, acquisitions, development and redevelopment of apartment communities.

**Table of Contents****Liquidity and Capital Resources (continued)***Dividend Reinvestment and Direct Stock Purchase Plan ( DRIP )*

The Company's DRIP provides the stockholders of the Company an opportunity to automatically invest their cash dividends in additional shares of common stock. In addition, eligible participants may make monthly payments or other voluntary cash investments in shares of common stock. The maximum monthly investment permitted without prior Company approval is currently \$10,000. The Company meets share demand under the DRIP through stock repurchases by the transfer agent in the open market on the Company's behalf or new stock issuances. Management monitors the relationship between the Company's stock price and its estimated net asset value ( NAV ). During times when the difference between these two values is small, resulting in little dilution of NAV by common stock issuances, the Company can choose to issue new shares. At times when the gap between NAV and stock price is greater, the Company has the flexibility to satisfy the demand for DRIP shares with stock repurchased by the transfer agent in the open market. In addition, the Company can issue waivers to DRIP participants to provide for investments in excess of the \$10,000 maximum monthly investment. No such waivers were granted during 2009 and through September 30, 2010.

*Stock Repurchase Program*

In 1997, the Company's Board of Directors (the Board ) approved a stock repurchase program under which the Company may repurchase shares of its common stock or UPREIT Units ( Company Program ). The shares and units may be repurchased through open market or privately negotiated transactions at the discretion of Company management. The Board's action did not establish a target stock price or a specific timetable for repurchase. There were no repurchases under the Company Program during 2009 and through September 30, 2010. The remaining authorization level as of September 30, 2010 is 2,291,160 shares. The Company will continue to monitor stock prices relative to the NAV to determine the current best use of capital among our major uses of capital: stock buybacks, debt paydown to increase the unencumbered pool, acquisitions, rehabilitation and/or redevelopment of owned properties and development of new properties. At the present time, the Company has no intention of buying any stock back during the remainder of 2010.

**Variable Interest Entities**

Through October 12, 2010, the Company was the general partner in one variable interest entity ( VIE ), syndicated using low income housing tax credits under Section 42 of the Internal Revenue Code. As general partner, the Company managed the day-to-day operations of the partnership for a management fee. In addition, the Company had an operating deficit guarantee and tax credit guarantee to the limited partner of that partnership. The Company was responsible to fund operating deficits to the extent there were any and could receive operating incentive awards if cash flows reached certain levels. Included in the Consolidated Balance Sheet for the VIE as of September 30, 2010 are total assets of \$9.9 million, total liabilities of \$16.6 million and partners' deficit of \$6.7 million. Of the \$16.6 million in total liabilities, \$15.8 million represents non-recourse mortgage debt. The VIE is included in the Consolidated Statement of Operations for the three and nine months ended September 30, 2010 and 2009.

The Company, through its general partnership interest in the VIE, has guaranteed the low income housing tax credits to the limited partners for a remaining period of six years totaling approximately \$3 million. Such guarantee requires the Company to operate the property in compliance with Internal Revenue Code Section 42 for a total of 15 years. The Company believes the property's operations conform to the applicable requirements as set forth above. In addition, as the general partner in this partnership, the Company was obligated to advance funds to meet partnership operating deficits.

On October 13, 2010, the Company sold its general partnership interest in the VIE. The sale price included the assumption of the existing mortgage debt of \$15.8 million and \$0.05 million cash. In connection with this transaction, the Company will realize a gain of approximately \$0.5 million during the fourth quarter of 2010 and will no longer be obligated to fund operating deficits.

**Table of Contents****Acquisitions and Development***Acquisitions*

On April 1, 2010, the Company acquired two communities with a total of 318 units, Middlebrooke and Westbrooke, located in the Baltimore region from the same seller for a cash purchase price of \$23.7 million. In connection with these acquisitions, closing costs of \$0.2 million were incurred and are included in other expenses. Middlebrooke was built between 1974 and 1977, and consists of 168 garden units in nine three-story buildings and 40 townhomes. Westbrooke was built between 1961 and 1970, and contains five buildings, each with 22 units. The weighted average first year capitalization rate projected by the Company on these acquisitions was 6.3% after allocating 3% of rental revenues for management and overhead expenses and before normalized capital expenditures.

On June 17, 2010, the Company acquired Annapolis Roads, a 282 unit community in Annapolis, Maryland, which it had managed for the prior owner since 2000. The total purchase price of \$32.5 million included the assumption of an existing \$20.0 million fixed rate mortgage, \$7.5 million in cash and \$4.8 million in UPREIT Units. Closing costs of \$0.4 million were incurred and are included in other expenses. The property was built in three phases between 1974 and 1979 and consists of eleven residential buildings. The weighted average first year capitalization rate projected by the Company on this acquisition was 6.6%.

On July 29, 2010, the Company acquired The Greens at Columbia, a 168 unit community in Columbia, Maryland for a total purchase price of \$25.6 million. Consideration for the purchase included the assumption of an existing \$9.6 million fixed-rate mortgage and \$16.0 million in cash. Closing costs of \$0.3 million were incurred and are included in other expenses. The property, built in 1986 and 1987, includes fourteen, three-story, brick, garden style buildings. The weighted average first year capitalization rate projected by the Company on this acquisition was 6.1%.

On August 5, 2010, the Company acquired Village at Potomac Falls, a 247 unit apartment community located in Sterling, Virginia for a total cash purchase price of \$38.5 million. Closing costs of \$0.2 million were incurred and are included in other expenses. The garden style property, completed in 1999, consists of ten, three- and four-story buildings. The weighted average first year capitalization rate projected by the Company on this acquisition was 5.6%.

On September 30, 2010, the Company acquired Charleston Place, an 858 unit apartment community located in Ellicott City, Maryland for a total purchase price of \$103 million. Consideration for the purchase included the assumption of fixed-rate debt totaling \$70.8 million, with the remainder paid in cash. Closing costs of \$1.2 million were incurred and are included in other expenses. The property, built in three phases between 1971 and 1983, includes 26 three-story garden style buildings. The weighted average first year capitalization rate projected by the Company on this acquisition was 6.2%.

On September 30, 2010, the Company acquired The Courts at Fair Oaks, a 364 unit apartment community located in Fairfax, Virginia for a total purchase price of \$70.1 million. Consideration for the purchase included the assumption of an existing \$46 million fixed-rate mortgage, with the remainder paid in cash. Closing costs of \$0.3 million were incurred and are included in other expenses. The property was built in 1990 and contains 15 three-story garden style buildings within a gated community. The weighted average first year capitalization rate projected by the Company on this acquisition was 5.9%.

On September 30, 2010, the Company acquired Crescent Club, a 257 unit apartment community located in Suffolk County, Long Island, New York for a total cash purchase price of \$31.3 million. Closing costs of \$0.3 million were incurred and are included in other expenses. The property was built in 1973 and consists of 40 two-story garden style buildings within a gated community. The weighted average first year capitalization rate projected by the Company on this acquisition was 6.2%.

After the close of the third quarter, on October 18, 2010, the Company acquired a 120 unit apartment community located in Aurora, Illinois, a suburb of Chicago, for a total purchase price of \$14.5 million. In connection with this acquisition, closing costs of approximately \$0.1 million were incurred and will be included in other expenses for the fourth quarter of 2010. The property was built in 1996 and consists of 14 two-story garden style buildings. The weighted average first year capitalization rate projected by the Company on this acquisition was 6.2%.



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**Acquisitions and Development (continued)**

On a year to date basis, through October 31, 2010, the Company has acquired nine communities with 2,614 units for a combined purchase price of \$339.1 million.

*Development*

The Company has two projects currently under construction: 1200 East West Highway located in Silver Spring, Maryland, a 14-story high rise with 247 apartment units; and, the Courts at Huntington Station, located in Alexandria, Virginia, consisting of four four-story buildings with 421 apartment units.

During the second quarter of 2010, construction activities on 1200 East West Highway neared completion and the project experienced initial occupancy. As of September 30, 2010, all 247 units were available to rent, with 189 units occupied and another 14 units pre-leased. Full stabilization is anticipated by year-end.

During the second quarter of 2010, construction of the 202 units in Phase One of the Courts at Huntington Station neared completion. Initial occupancy was experienced in May 2010. As of September 30, 2010, there were 202 units available to rent, with 115 units occupied and another 14 units pre-leased. The lease-up period is projected to last eleven months. Construction on Phase Two, consisting of 219 units, has commenced and is scheduled to be completed in the second quarter of 2011, reaching stabilized occupancy approximately one year later.

The Company also has two projects in pre-construction development: Cobblestone Square located in Fredericksburg, Virginia, consisting of approximately 314 apartment units; and Ripley Street located in Silver Spring, Maryland, an 18-story high rise with approximately 379 apartment units. Both projects are on entitled land that the Company purchased from other developers and both are in the final stages of the design process.

**Contractual Obligations and Other Commitments**

The primary obligations of the Company relate to its borrowings under the line of credit, Senior Notes and mortgage notes payable. The Company's line of credit matures in August 2011 (not including a one-year optional extension) and had \$137.0 million in loans, and letters of credit totaling \$4.4 million, outstanding at September 30, 2010. The \$2.3 billion in mortgage notes payable have varying maturities ranging from 3 months to 24 years. The weighted average interest rate of the Company's secured debt was 5.32% at September 30, 2010. The weighted average rate of interest on the Company's total indebtedness of \$2.6 billion at September 30, 2010 was 5.30%.

In October 2006, the Company issued \$200 million of Senior Notes with a coupon rate of 4.125%. During 2008, the Company repurchased and retired \$60 million principal amount of its Senior Notes and \$140 million remain outstanding at September 30, 2010. The notes are exchangeable into cash equal to the principal amount of the notes and, at the Company's option, cash or common stock for the exchange value, to the extent that the market price of common stock exceeds the initial exchange price of \$73.34 per share, subject to adjustment. The exchange price is adjusted for payments of dividends in excess of the reference dividend set in the indenture of \$0.64 per share. The adjusted exchange price at September 30, 2010 was \$72.87 per share. Upon an exchange of the notes, the Company will settle any amounts up to the principal amount of the notes in cash and the remaining exchange value, if any, will be settled, at the Company's option, in cash, common stock or a combination of both. The notes are not redeemable at the option of the Company for five years from their issue date, except to preserve the status of the Company as a REIT. Holders of the notes may require the Company to repurchase the notes upon the occurrence of certain designated events. In addition, prior to November 1, 2026, the holders may require the Company to repurchase the notes on November 1, 2011, 2016 and 2021. The notes will mature on November 1, 2026, unless previously redeemed, repurchased or exchanged in accordance with their terms prior to that date.

The Company leases its corporate office space from an affiliate and the office space for its regional offices from non-affiliated third parties. The rent for the corporate office space is a gross rent that includes real estate taxes and common area maintenance. The regional office leases are net leases which require an annual base rent plus a pro-rata portion of real estate taxes.

**Table of Contents****Capital Improvements** (dollars in thousands, except unit and per unit data)

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 and bath cabinets, new roofs, site improvements and various exterior building improvements. Non-recurring, revenue generating upgrades include community centers, new windows, and kitchen and bath apartment upgrades. Revenue generating capital improvements are expected to directly result in increased 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 \$800 per unit is spent on recurring capital expenditures in 2010 and 2009. During the three months ended September 30, 2010 and 2009, approximately \$200 per unit was spent on recurring capital expenditures; and for the nine months ended September 30, 2010 and 2009, approximately \$600 per unit was spent on recurring capital expenditures.

The table below summarizes the actual total capital improvements incurred by major categories for the three and nine months ended September 30, 2010 and 2009 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 months ended September 30, 2010 as follows:

	For the three months ended September 30,						2009	
	2010		2010		2010		2009	
	Recurring	Per	Non-	Per	Total	Per	Total	Per
	Cap	Unit <sup>(a)</sup>	Recurring	Unit <sup>(a)</sup>	Capital	Unit <sup>(a)</sup>	Capital	Unit <sup>(a)</sup>
	Ex		Cap Ex		Improvements		Improvements	
	\$	\$	\$	\$	\$	\$	\$	\$
New buildings			9		9		34	1
Major building								
improvements	1,156	32	3,329	91	4,485	123	3,294	92
Roof replacements	303	8	1,032	28	1,335	36	656	18
Site improvements	404	11	2,922	80	3,326	91	2,081	58
Apartment upgrades	1,226	33	8,248	225	9,474	258	5,678	159
Appliances	1,389	38			1,389	38	1,201	34
Carpeting/flooring	2,027	55	1,194	33	3,221	88	2,891	81
HVAC/mechanicals	651	18	3,904	106	4,555	124	2,245	63
Miscellaneous	183	5	678	18	861	23	175	5
Totals	\$ 7,339	\$ 200	\$ 21,316	\$ 581	\$ 28,655	\$ 781	\$ 18,255	\$ 511

(a) Calculated using the weighted average number of units owned, including 35,798 core units and 2010 acquisition units

of 892 for the  
three months  
ended  
September 30,  
2010; and  
35,798 core  
units for the  
three months  
ended  
September 30,  
2009.

**Table of Contents****Capital Improvements (continued)**

	For the nine months ended September 30,						2009	
	2010		2010		2010		2009	
	Recurring Cap Ex	Per Unit <sup>(a)</sup>	Non- Recurring Cap Ex	Per Unit <sup>(a)</sup>	Total Capital Improvements	Per Unit <sup>(a)</sup>	Total Capital Improvements	Per Unit <sup>(a)</sup>
New buildings	\$	\$	\$ 93	\$ 3	\$ 93	\$ 3	\$ 630	\$ 18
Major building improvements	3,423	95	6,087	168	9,510	263	9,602	268
Roof replacements	896	25	1,408	39	2,304	64	2,093	58
Site improvements	1,195	33	5,605	155	6,800	188	3,771	105
Apartment upgrades	4,034	111	18,000	497	22,034	608	17,362	485
Appliances	3,708	102			3,708	102	3,385	95
Carpeting/flooring	6,003	166	1,704	47	7,707	213	7,942	222
HVAC/mechanicals	1,929	53	9,738	269	11,667	322	6,079	170
Miscellaneous	543	15	1,190	33	1,733	48	1,452	41
Totals	\$ 21,731	\$ 600	\$ 43,825	\$ 1,211	\$ 65,556	\$ 1,811	\$ 52,316	\$ 1,462

(a) Calculated using the weighted average number of units owned, including 35,798 core units and 2010 acquisition units of 422 for the nine months ended September 30, 2010; and 35,798 core units for the nine months ended September 30, 2009.

The schedule below summarizes the breakdown of total capital improvements between core and non-core as follows:

	For the three months ended September 30,						2009	
	2010		2010		2010		2009	
	Recurring Cap Ex	Per Unit <sup>(b)</sup>	Non- Recurring Cap Ex	Per Unit <sup>(b)</sup>	Total Capital Improvements	Per Unit <sup>(b)</sup>	Total Capital Improvements	Per Unit <sup>(b)</sup>



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Core Communities	\$ 7,161	\$ 200	\$ 20,997	\$ 587	\$ 28,158	\$ 787	\$ 18,255	\$ 511
2010 Acquisition Communities	178	200	319	358	497	558		
Sub-total	7,339	200	21,316	581	28,655	781	18,255	511
2009 Disposed Communities							126	213
Corporate office expenditures <sup>(1)</sup>					452		464	
Totals	\$ 7,339	\$ 200	\$ 21,316	\$ 581	\$ 29,107	\$ 781	\$ 18,845	\$ 505

(1) No distinction is made between recurring and non-recurring expenditures for corporate office. Corporate office expenditures include principally computer hardware, software, office furniture, fixtures and leasehold improvements.

(b) Calculated using the weighted average number of units owned, including 35,798 core units and 2010 acquisition units of 892 for the three months ended September 30, 2010; and 35,798 core units and 2009 disposed units of 592 for the three months ended

September 30,  
2009.

**Table of Contents****Capital Improvements (continued)**

	For the nine months ended September 30,						2009	
	2010		2010		2010		2009	
	Recurring Cap Ex	Per Unit <sup>(b)</sup>	Non- Recurring Cap Ex	Per Unit <sup>(b)</sup>	Total Capital Improvements	Per Unit <sup>(b)</sup>	Total Capital Improvements	Per Unit <sup>(b)</sup>
Core Communities	\$ 21,478	\$ 600	\$ 43,486	\$ 1,215	\$ 64,964	\$ 1,815	\$ 52,316	\$ 1,462
2010 Acquisition Communities	253	600	339	803	592	1,403		
Sub-total	21,731	600	43,825	1,211	65,556	1,811	52,316	1,462
2009 Disposed Communities							618	918
Corporate office expenditures <sup>(1)</sup>					2,427		1,226	
Totals	\$ 21,731	\$ 600	\$ 43,825	\$ 1,211	\$ 67,983	\$ 1,811	\$ 54,160	\$ 1,451

(1) No distinction is made between recurring and non-recurring expenditures for corporate office. Corporate office expenditures include principally computer hardware, software, office furniture, fixtures and leasehold improvements.

(b) Calculated using the weighted average number of units owned, including 35,798 core units, and 2010 acquisition units of 422 for the nine months

ended  
September 30,  
2010; and  
35,798 core  
units and 2009  
disposed units  
of 673 for the  
nine months  
ended  
September 30,  
2009.

Results of Operations (dollars in thousands, except unit and per unit data)

Net operating income ( NOI ) may fall within the definition of non-GAAP financial measure set forth in Item 10(e) of Regulation S-K and, as a result, the Company may be required to include in this report a statement disclosing the reasons why management believes that presentation of this measure provides useful information to investors. The Company believes that NOI is helpful to investors as a supplemental measure of the operating performance of a real estate company because it is a direct measure of the actual operating results of the Company's apartment communities. In addition, the apartment communities are valued and sold in the market by using a multiple of NOI. The Company uses this measure to compare its performance to that of its peer group.

*Summary of Core Properties*

The Company had 105 apartment communities with 35,798 units which were owned during the three and nine months ended September 30, 2010 and 2009 (the Core Properties ). The Company has acquired eight apartment communities with 2,494 units and has placed into service another 449 units at two development communities during 2010 (the Acquisition Communities ). During 2009, the Company disposed of five apartment communities with a total of 1,333 units, which had partial results for 2009 (the 2009 Disposed Communities ). The results of these disposed properties have been classified as discontinued operations and are not included in the table below.

The inclusion of the Acquisition Communities generally accounted for the significant changes in operating results for the three and nine months ended September 30, 2010. In addition, the reported income from operations include the results of one investment where the Company is the managing general partner that has been determined to be a VIE and consolidated with the Company. The general partnership interest was sold on October 13, 2010, after the end of the third quarter.

**Table of Contents****Results of Operations (continued)**

A summary of the net operating income for Core Properties is as follows:

	Three Months				Nine Months			
	2010	2009	\$ Change	% Change	2010	2009	\$ Change	% Change
Rent	\$ 114,872	\$ 114,467	\$ 405	0.4%	\$ 342,393	\$ 343,684	\$ (1,291)	(0.4%)
Utility recovery revenue	3,853	3,526	327	9.3%	15,304	14,450	854	5.9%
Rent including recoveries	118,725	117,993	732	0.6%	357,697	358,134	(437)	(0.1%)
Property other income	5,625	5,640	(15)	(0.3%)	16,036	15,775	261	1.7%
Total revenue	124,350	123,633	717	0.6%	373,733	373,909	(176)	(0.0%)
Operating and maintenance	(48,539)	(50,346)	1,807	3.6%	(153,316)	(155,762)	2,446	1.6%
Net operating income	\$ 75,811	\$ 73,287	\$ 2,524	3.4%	\$ 220,417	\$ 218,147	\$ 2,270	1.0%

A summary of the net operating income for the Company as a whole is as follows:

	Three Months				Nine Months			
	2010	2009	\$ Change	% Change	2010	2009	\$ Change	% Change
Rent	\$ 120,067	\$ 115,611	\$ 4,456	3.9%	\$ 351,006	\$ 347,111	\$ 3,895	1.1%
Utility recovery revenue	3,904	3,526	378	10.7%	15,366	14,460	906	6.3%
Rent including recoveries	123,971	119,137	4,834	4.1%	366,372	361,571	4,801	1.3%
Property other income	5,777	5,656	121	2.1%	16,286	15,810	476	3.0%
Total revenue	129,748	124,793	4,955	4.0%	382,658	377,381	5,277	1.4%
Operating and maintenance	(51,361)	(51,302)	(59)	(0.1%)	(159,050)	(158,702)	(348)	(0.2%)
Net operating income	\$ 78,387	\$ 73,491	\$ 4,896	6.7%	\$ 223,608	\$ 218,679	\$ 4,929	2.3%

*Comparison of three months ended September 30, 2010 to the same period in 2009*

Of the \$4,456 increase in rental income, \$4,051 is attributable to the Acquisition Communities and a \$405 increase from the Core Properties as the result of an increase of 0.2% in weighted average rental rates from \$1,138 to \$1,140 per apartment unit; and by a 0.1% increase in economic occupancy from 93.7% to 93.8%. Economic 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 rents and vacant units at

market rents. Of the \$378 increase in utility recovery revenue, \$327 is attributable to the Core Properties, and \$51 is attributable to the Acquisition Communities.

Property other income, which consists primarily of income from operation of laundry facilities, late charges, administrative fees, garage and carport rentals, revenue from corporate apartments, cable revenue, pet charges, and miscellaneous charges to residents, increased by \$121. Of this increase, \$136 is attributable to the Acquisition Communities partially offset by a \$15 decrease attributable to the Core Properties due mainly to a leveling off of lease break fees in the current period.

Of the \$59 increase in operating and maintenance expenses, \$1,866 is attributable to the Acquisition Communities, offset by a \$1,807 decrease attributable to the Core Properties. The decrease in Core Properties is primarily due to decreases in property insurance, repairs and maintenance expense, real estate taxes and natural gas heating costs, partially offset by increases in personnel expense, and water and sewer costs.

Property insurance decreased by \$1,257, or 55.2%, primarily from \$794 lower property and general liability losses in 2010 as compared to 2009 due in part to the timing of the property aggregate retention funding, which occurred earlier in 2010 than 2009; plus the favorable impact in 2010 of property level safety and loss prevention measures. In addition, there was a \$276 favorable impact between periods as a result of required prior period reserve decreases, which were \$631 in 2010 as compared to \$355 in 2009. The continuing reserve decreases are a direct result of the Company's focus on settling older claims where the number of open claims has dropped 23% and 24% in 2010 and 2009, respectively. The lower number of open claims had a favorable impact on the estimated required reserves in both 2010 and 2009.

**Table of Contents****Results of Operations (continued)**

Repairs and maintenance expenses were down \$560, or 6.5% from a year ago due partly to a \$653 recovery from an insurance claim in 2010 compared to a \$214 recovery in 2009. Without the impact of the insurance recoveries, the recurring repairs & maintenance expenses decreased \$121, or 1.4%, which reflects cost savings realized through the rebidding of selected service contracts resulting in reduced rates in this more competitive economic environment and the favorable impact of lower resident turnover of 11.8% in 2010 as compared to 12.1% in 2009, which resulted in less spending on apartment turnover costs.

Real estate taxes decreased \$512, or 4.2%, due to tax assessment refunds in 2010 of \$571 as compared to none in 2009. After removing the effects of these refunds, real estate taxes were up \$59, or 0.5%.

Natural gas heating costs were down \$100, or 6.5% from a year ago due to lower commodity rates partially offset by higher consumption. For the third quarter 2010, our natural gas weighted average cost, including transportation of \$3.00 per decatherm, was \$9.18 per decatherm, compared to \$10.69 per decatherm for the 2009 period, a 14.1% decrease.

Personnel costs increased \$406, or 3.4%, primarily due to increasing the 2008 and prior year workers compensation retention reserves by \$274 in 2010 compared to an increase of \$20 to the workers compensation reserves in 2009. Beginning in 2009, the Company entered into guaranteed cost programs for its workers compensation insurance. Without the impacts of the insurance reserve adjustments, personnel costs increased \$152, or 1.3%.

Water and sewer costs increased \$335, or 8.7%, due to municipalities increasing rates and a 1.7% increase in usage.

General and administrative expenses decreased in 2010 by \$548, or 9.0%. General and administrative expenses as a percentage of total revenues were 4.3% for 2010 as compared to 4.9% for 2009. Stock-based compensation costs were down \$541 due to the true-up of estimated stock option forfeitures for the 2004 grant year occurring in the third quarter of 2009 as compared to the 2005 grant year forfeiture estimate being trueed-up in the second quarter of 2010. This is a result of the Company changing the month of grant to May beginning in 2005 from August in 2004.

Interest expense increased by \$325, or 1.1% in 2010 primarily as a result of a higher level borrowings in 2010 as compared to 2009 partially offset by a lower average interest rate of 5.30% in 2010, which is 32 basis points lower than the 2009 average rate due in part to recent borrowings and refinancing at rates averaging 4.65%.

Depreciation and amortization expense increased \$2,418, or 8.1% due to the depreciation on the Acquisition Communities and the capital additions to the Core Properties.

Other expenses of \$2,213 are the 2010 property acquisition costs from the five acquisitions closed in the third quarter of 2010.

Included in discontinued operations for the three months ended September 30, 2010, are the residual operating results of the 2009 Disposed Communities.

*Comparison of nine months ended September 30, 2010 to the same period in 2009*

Of the \$3,895 increase in rental income, \$5,186 is attributable to the Acquisition Communities; partially offset by a decrease of \$1,291 attributable to the Core Properties as the result of a 0.8% decrease in weighted average rental rates from \$1,141 to \$1,132 per apartment unit; partially offset by a 0.4% increase in economic occupancy from 93.5% to 93.9%. Of the \$906 increase in utility recovery revenue, \$854 is attributable to the Core Properties and is partially driven by a comparable increase in water and sewer expense.

Property other income, which consists primarily of income from operation of laundry facilities, late charges, administrative fees, garage and carport rentals, revenue from corporate apartments, cable revenue, pet charges, and miscellaneous charges to residents, increased by \$476. Of this increase, \$215 is attributable to the Acquisition Communities and \$261 is attributable to the Core Properties resulting primarily from increases in cable revenue and renters insurance door fees.

**Table of Contents****Results of Operations (continued)**

Of the \$348 increase in operating and maintenance expenses, \$2,794 is attributable to the Acquisition Communities, offset by a \$2,446 decrease attributable to the Core Properties. The decrease in Core Properties is primarily due to decreases in natural gas heating costs, repairs and maintenance, property insurance and electricity; partially offset by increases in snow removal costs and water and sewer costs.

Natural gas heating costs were down \$2,010, or 14.9% from a year ago due to a combination of lower commodity rates offset by increased consumption resulting from a slightly colder 2010 than 2009. For 2010, the Company's natural gas weighted average cost, including transportation of \$3.00 per decatherm, was \$9.31 per decatherm, compared to \$11.10 per decatherm for the 2009 period, a 16.1% decrease.

Repairs and maintenance expenses were down \$1,235, or 5.4% from a year ago due partly to insurance claim recoveries of \$783 in 2010 compared to \$417 in 2009. Without the impact of the insurance recoveries, the recurring repairs & maintenance expenses decreased \$869, or 3.8%, which reflects cost savings realized through the rebidding of selected service contracts resulting in reduced rates in this more competitive economic environment and the favorable impact of lower resident turnover of 29.8% in 2010 as compared to 30.9% in 2009, which resulted in less spending on apartment turnover costs.

Property insurance decreased by \$597, or 9.0%, primarily from \$2,082 lower property and general liability losses in 2010 as compared to 2009 due in part to the timing of the property aggregate retention funding, which occurred in December 2009 for the 2009/2010 insurance policy year as a result of two major fire losses, plus the favorable impact in 2010 of property level safety and loss prevention measures. In addition, there were favorable impacts realized in both periods as a result of required prior period reserve decreases, which were \$607 and \$617 in 2010 and 2009, respectively. These reserve decreases are a direct result of the Company focus on settling older claims where the number of open claims has dropped 23% and 24% in 2010 and 2009, respectively. The lower number of open claims had a favorable impact on the estimated required reserves in both 2010 and 2009. The 2009 period also realized the benefit of \$503 in subrogation counterclaims settled for prior year property and general liability losses.

Electricity costs were down \$529, or 7.6% from a year ago primarily as a result of several energy conservation efforts including a compact fluorescent bulb replacement program that was rolled out in the third quarter of 2009. In addition, suppliers were changed in the Boston and Long Island regions in 2010 resulting in savings along with receiving one time rebates of \$229 in the Baltimore and Washington D.C. regions.

Snow removal costs were up \$1,243, or 171%, as most of our Mid-Atlantic region properties suffered from record storms in the first quarter 2010.

Water and sewer costs increased \$848, or 7.9%, due to rate increases by municipalities and a 1.7% increase in usage.

General and administrative expenses decreased in 2010 by \$17, or 0.1%. General and administrative expenses as a percentage of total revenues were 4.8% for both 2010 and 2009. The incentive bonus increased \$264 compared to 2009, which reflects the relative increase in the Company's operating performance versus its peers as compared to the prior year. Stock based compensation expenses were up \$348 in 2010 as compared to 2009, primarily due to the impact of employees nearing retirement vesting over one less year in 2010 as compared to 2009. These increases were partially offset by the 2009 period containing nonrecurring severance costs in the amount of \$606.

Interest expense decreased by \$124 or 0.1% in 2010 primarily as a result of a higher level of variable interest rate borrowings in 2010 as compared to 2009, which yielded lower effective rates than the fixed rate debt.

Depreciation and amortization expense increased \$4,276, or 4.8% due to the depreciation on the Acquisition Communities and the capital additions to the Core Properties.

Other expenses of \$2,804 are the 2010 property acquisition costs from the eight acquisitions closed in 2010 and \$32 in pursuit costs incurred in connection with deals that were abandoned.



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**Results of Operations (continued)**

Included in discontinued operations for the nine months ended September 30, 2010, are the residual operating results of the 2009 Disposed Communities. For purposes of the discontinued operations presentation, the Company only includes interest expense and losses from early extinguishment of debt associated with specific mortgage indebtedness of the properties that are sold or held for sale.

**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, noncontrolling interest, extraordinary items and cumulative effect of change in accounting principle plus depreciation from real property including adjustments for unconsolidated partnerships and joint ventures less dividends from non-convertible preferred shares. 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.

In addition to presenting FFO in accordance with the NAREIT definition, we also disclose FFO after a specific and defined supplemental adjustment to exclude losses from early extinguishments of debt associated with the sales of real estate ( FFO as adjusted ). The adjustment to exclude losses from early extinguishments of debt results when the sale of real estate encumbered by debt requires us to pay the extinguishment costs prior to the debt's stated maturity and to write-off unamortized loan costs at the date of the extinguishment. Such costs are excluded from the gains on sales of real estate reported in accordance with GAAP. However, we view the losses from early extinguishments of debt associated with the sales of real estate as an incremental cost of the sale transactions because we extinguished the debt in connection with the consummation of the sale transactions and we had no intent to extinguish the debt absent such transactions. We believe that this supplemental adjustment more appropriately reflects the results of our operations exclusive of the impact of our sale transactions.

Although our FFO as adjusted clearly differs from NAREIT's definition of FFO, and may not be comparable to that of other REITs and real estate companies, we believe it provides a meaningful supplemental measure of our operating performance because we believe that, by excluding the effects of the losses from early extinguishments of debt associated with the sales of real estate, management and investors are presented with an indicator of our operating performance that more closely achieves the objectives of the real estate industry in presenting FFO.

Neither FFO, nor FFO as adjusted, should be considered as an alternative to net income (determined in accordance with GAAP) as an indication of our performance. Neither FFO, nor FFO as adjusted represents cash generated from operating activities determined in accordance with GAAP, and neither is a measure of liquidity or an indicator of our ability to make cash distributions. We believe that to further understand our performance, FFO, and FFO as adjusted should be compared with our reported net income and considered in addition to cash flows in accordance with GAAP, as presented in our consolidated financial statements.

FFO and FFO as adjusted fall within the definition of non-GAAP financial measure set forth in Item 10(e) of Regulation S-K and as a result the Company is required to include in this report a statement disclosing the reasons why management believes that presentation of this measure provides useful information to investors. Management believes that in order to facilitate a clear understanding of the consolidated historical operating results of the Company, FFO, and FFO as adjusted 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 and FFO as adjusted can help one compare the operating performance of a company's real estate between periods or as compared to different companies. In addition, FFO as adjusted ties the losses on early extinguishment of debt to the real estate which was sold triggering the extinguishment. The Company also uses these measures to compare its performance to that of its peer group.



**Table of Contents****Funds From Operations (continued)**

The calculation of FFO and reconciliation to GAAP net income attributable to common stockholders for the three and nine months ended September 30, 2010 and 2009 are presented below (in thousands):

	Three Months		Nine Months	
	2010	2009	2010	2009
Net income attributable to common stockholders	\$ 5,507	\$ 5,264	\$ 13,312	\$ 22,186
Real property depreciation and amortization	31,722	29,712	91,691	88,763
Noncontrolling interest	1,695	1,956	4,180	8,375
Loss (gain) on disposition of property		22	13	(13,471)
FFO Basic and Diluted, as defined by NAREIT	38,924	36,954	109,196	105,853
Loss from early extinguishment of debt in connection with sale of real estate				4,927
FFO Basic and Diluted, as adjusted by the Company	\$ 38,924	\$ 36,954	\$ 109,196	\$ 110,780
Weighted average common shares/units outstanding <sup>(1)</sup> :				
Basic	48,883.4	45,243.0	47,935.2	45,220.8
Diluted	49,389.7	45,361.9	48,376.7	45,284.7

(1) Basic includes common stock outstanding plus UPREIT Units which can be converted into shares of common stock. Diluted includes additional common stock equivalents.

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**

The credit agreement relating to the Company's line of credit provides for the Company to maintain certain financial covenants. The Company was in compliance with these financial covenants for all periods presented. The line of credit has not been used for long-term financing but adds a certain amount of flexibility, especially in meeting the Company's acquisition goals. Many times it is easier to temporarily finance an acquisition or stock repurchases by short-term use of the line of credit, with long-term secured financing or other sources of capital replenishing the line of credit availability.

**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. In

response to the current economic climate, the Company may also elect to hold or slightly reduce rents in order to remain competitive and retain occupancy in certain markets. These short-term leases minimize the potential adverse effect of inflation or deflation 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 the fourth quarter of 2007, throughout 2008, 2009 and continuing into 2010, the sub-prime issue put significant pressure on the mortgage lending industry. Despite this, the Company has continued to receive favorable financing at market rates of interest. Its physical occupancy at 95.0% in 2008, 94.9% in 2009 and 95.2% during the first three quarters of 2010 remain the highest it has been since 2000 and financial performance continued strong. However, a recessionary economy and high unemployment typically slow household formations which could affect occupancy and decrease the Company's ability to raise rents. In light of this, we will continue to review our business strategy throughout the year. However, we believe that given our B-class property type and the geographic regions in which we are located, the Company's financial performance will be affected less negatively than its peers.

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**Dividends and Distributions**

On October 26, 2010, the Board of Directors declared a dividend of \$0.58 per share on the Company's common stock and approved a distribution of \$0.58 per UPREIT Unit for the quarter ended September 30, 2010. This is the equivalent of an annual distribution of \$2.32 per share/unit. The dividend and distribution is payable November 23, 2010, to stockholders and unitholders of record on November 12, 2010.

**Contingencies**

The Company is not a party to any legal proceedings which are expected to have a material adverse effect on the Company's liquidity, financial position or results of operations. The Company is subject to a variety of legal actions for personal injury or property damage arising in the ordinary course of its business, most of which are covered by liability and property insurance. Various claims of employment and resident discrimination are also periodically brought, most of which also are covered by insurance. While the resolution of these matters cannot be predicted with certainty, management believes that the final outcome of such legal proceedings and claims will not have a material adverse effect on the Company's liquidity, financial position or results of operations.

**Recently Adopted and Recently Issued Accounting Standards**

Disclosure of recently adopted and recently issued accounting standards is incorporated herein by reference to the discussion under Part I, Item 1, Notes to Consolidated Financial Statements, Note 3.

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## 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, 2010 and December 31, 2009, approximately 86% and 89%, respectively, of the Company's debt bore interest at fixed rates. At September 30, 2010 and December 31, 2009, approximately 80% and 83%, respectively, of the Company's debt was secured and bore interest at fixed rates. The secured fixed rate debt had weighted average maturities of approximately 5.53 years and 5.35 years and a weighted average interest rate of approximately 5.59% and 5.86% at September 30, 2010 and December 31, 2009, respectively. The remainder of the Company's secured debt bore interest at variable rates with a weighted average maturity of approximately 6.66 and 7.75 years and a weighted average interest rate of 2.97% and 2.92% at September 30, 2010 and December 31, 2009, respectively. The Company does not intend to utilize a significant amount of permanent variable rate debt to acquire properties in the future. On occasion, the Company may use its line of credit in connection with a property acquisition or stock repurchase with the intention to refinance at a later date. The Company believes that increases in interest expense as a result of inflation would not significantly impact the Company's distributable cash flow.

At September 30, 2010 and December 31, 2009, the fair value of the Company's fixed and variable rate secured debt amounted to a liability of \$2.50 billion and \$2.15 billion, respectively, compared to its carrying amount of \$2.32 billion and \$2.11 billion, respectively. The Company estimates that a 100 basis point increase in market interest rates at September 30, 2010 would have changed the fair value of the Company's fixed and variable rate secured debt to a liability of \$2.39 billion and would result in \$2.4 million higher interest expense on the variable rate secured debt on an annualized basis. At September 30, 2010 and December 31, 2009, the fair value of the Company's total debt, including the Senior Notes and line of credit, amounted to a liability of \$2.77 billion and \$2.34 billion, respectively, compared to its carrying amount of \$2.60 billion and \$2.30 billion.

The Company intends to continuously monitor and actively manage interest costs on its variable rate debt portfolio and may enter into swap positions based upon market fluctuations. Accordingly, the cost of obtaining such interest rate protection agreements in relation to 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. In addition, the Company believes that it has the ability to obtain funds through additional debt and/or equity offerings and/or the issuance of UPREIT Units. As of September 30, 2010, the Company had no other material exposure to market risk.

## ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports filed or submitted by the Company under the Securities Exchange Act of 1934 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 officers who certify the Company's financial reports and to the other members of senior management and the Board of Directors.

The principal executive officer and principal financial officer evaluated, as of September 30, 2010, the effectiveness of the disclosure controls and procedures (as defined in Rules 13a-15(e) and 15-d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) and have determined that such disclosure controls and procedures are effective.

There have been no changes in the internal controls over financial reporting identified in connection with that evaluation, or that occurred during the third quarter of the year ended December 31, 2010 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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HOME PROPERTIES, INC.  
PART II OTHER INFORMATION

ITEM 1A. RISK FACTORS

Refer to the Risk Factors disclosure in the Company's Form 10-K for the year ended December 31, 2009. There have been no material changes in these risk factors during the nine months ended September 30, 2010 and through the date of this report.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES; USE OF PROCEEDS FROM REGISTERED SECURITIES

Unregistered Sales of Equity Securities

None.

Issuer Purchases of Equity Securities

In 1997, the Company's Board of Directors (the Board) approved a stock repurchase program under which the Company may repurchase shares of its outstanding common stock and UPREIT Units (Company Program). The shares and units may be repurchased through open market or privately negotiated transactions at the discretion of Company management. The Board's action does not establish a specific target stock price or a specific timetable for share repurchase. In addition, participants in the Company's Stock Benefit Plan can use common stock of the Company that they already own to pay all or a portion of the exercise price payable to the Company upon the exercise of an option. In such event, the common stock used to pay the exercise price is returned to authorized but unissued status, and is deemed to have been repurchased by the Company. At September 30, 2010, the Company had authorization to repurchase 2,291,160 shares of common stock and UPREIT Units under the Company Program.

There were no shares (units) repurchased by the Company during the quarter ended September 30, 2010.

ITEM 6. EXHIBITS

Exhibit 31.1 Section 302 Certification of Chief Executive Officer\*

Exhibit 31.2 Section 302 Certification of Chief Financial Officer\*

Exhibit 32.1 Section 906 Certification of Chief Executive Officer\*\*

Exhibit 32.2 Section 906 Certification of Chief Financial Officer\*\*

Exhibit 101 XBRL (eXtensible Business Reporting Language). The following materials from the Home Properties, Inc. Quarterly Report on Form 10-Q for the period ended September 30, 2010, formatted in XBRL: (i) consolidated balance sheets, (ii) consolidated statements of operations, (iii) consolidated statements of equity, (iv) consolidated statements of cash flows and (v) notes to consolidated financial statements. As provided in Rule 406T of Regulation S-T, this information is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934. \*\*

\* Filed herewith

\*\* Furnished  
herewith

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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 5, 2010

By: /s/ Edward J. Pettinella

Edward J. Pettinella  
President and Chief Executive Officer

Date: November 5, 2010

By: /s/ David P. Gardner

David P. Gardner  
Executive Vice President and  
Chief Financial Officer