CAPITAL PROPERTIES INC /RI/
Form 10-Q
July 30, 2010

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 10-Q

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

For the quarterly period ended June 30, 2010

OR

o **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 001-08499

CAPITAL PROPERTIES, INC.

(Exact name of registrant as specified in its charter)

Rhode Island	**05-0386287**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

100 Dexter Road
East Providence, Rhode Island 02914
(Address of principal executive offices) (Zip Code)
(401) 435-7171
(Registrant s telephone number, including area code)
Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Class A Common Stock, $.01 par value	**OTCQX (Pink Sheets)**

Securities registered pursuant to Section 12(g) of the Act:
NONE

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company.

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

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

As of June 30, 2010, the Company had 3,721,411 shares of Class A Common Stock and 2,878,501 shares of Class B Common Stock outstanding.

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PART I

Item 1. Consolidated Financial Statements
CAPITAL PROPERTIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	June 30, 2010 (unaudited)	December 31, 2009
ASSETS		
Properties and equipment (net of accumulated depreciation)	$ 22,274,000	$ 22,069,000
Cash	2,712,000	2,315,000
Income taxes receivable	318,000	47,000
Prepaid and other	453,000	331,000
	$ 25,757,000	$ 24,762,000
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities:		
Note payable	$ 5,975,000	$
Accounts payable and accrued expenses:		
Property taxes	248,000	243,000
Environmental remediation	81,000	81,000
Other	511,000	514,000
Deferred:		
Leasing revenues	520,000	520,000
Income taxes, net	5,407,000	5,305,000
	12,742,000	6,663,000
Shareholders equity:		
Class A common stock, $.01 par; authorized 10,000,000 shares; issued and outstanding, 3,721,411 shares at June 30, 2010 and 3,654,739 shares at December 31, 2009	37,000	37,000
Class B common stock, $.01 par; authorized 3,500,000 shares; issued and outstanding, 2,878,501 shares at June 30, 2010 and 2,945,173 shares at December 31, 2009	29,000	29,000
Excess stock, $.01 par; authorized 1,000,000 shares; none issued and outstanding		
Capital in excess of par	11,762,000	11,762,000
Retained earnings	1,187,000	6,271,000
	13,015,000	18,099,000
	$ 25,757,000	$ 24,762,000

See notes to consolidated financial statements.

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CAPITAL PROPERTIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Three Months Ended June 30		Six Months Ended June 30	
	2010	2009	2010	2009
Revenues:				
Leasing	$ 775,000	$ 760,000	$ 1,490,000	$ 1,474,000
Petroleum storage facility	953,000	949,000	1,889,000	1,885,000
	1,728,000	1,709,000	3,379,000	3,359,000
Expenses:				
Leasing	228,000	204,000	564,000	407,000
Petroleum storage facility	602,000	647,000	1,131,000	1,224,000
General and administrative	226,000	231,000	492,000	490,000
Interest	64,000		64,000	
	1,120,000	1,082,000	2,251,000	2,121,000
Income before income taxes	608,000	627,000	1,128,000	1,238,000
Income tax expense (benefit):				
Current	114,000	267,000	236,000	522,000
Deferred	68,000	(12,000)	102,000	(22,000)
	182,000	255,000	338,000	500,000
Net income	$ 426,000	$ 372,000	$ 790,000	$ 738,000
Basic income per common share based upon 6,599,912 shares outstanding	$ .06	$ .06	$ .12	$ .11
Dividends per share on common stock based upon 6,599,912 shares outstanding	$ .86	$ .03	$ .89	$ .06

See notes to consolidated financial statements.

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CAPITAL PROPERTIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
SIX MONTHS ENDED JUNE 30, 2010 AND 2009
(Unaudited)

	2010	2009
Cash flows from operating activities:		
Net income	$ 790,000	$ 738,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	375,000	346,000
Deferred income taxes	102,000	(22,000)
Other, principally net changes in prepaids, accounts payable, accrued expenses and current income taxes	(135,000)	(461,000)
Net cash provided by operating activities	1,132,000	601,000
Cash used in investing activities, payments for properties and equipment	(781,000)	(287,000)
Cash flows from financing activities:		
Proceeds from note payable	6,000,000	
Payments:		
Note payable	(25,000)	
Deferred financing fees	(55,000)	
Dividends	(5,874,000)	(396,000)
Net cash provided by (used in) financing activities	46,000	(396,000)
Increase (decrease) in cash	397,000	(82,000)
Cash, beginning	2,315,000	3,395,000
Cash, ending	$ 2,712,000	$ 3,313,000
Supplemental disclosures:		
Cash paid for:		
Income taxes	$ 561,000	$ 941,000
Interest	$ 34,000	$
Non-cash investing and financing activities:		
Capital expenditures financed through accounts payable	$ 167,000	$ 115,000
Conversion of Class B Common Stock into Class A Common Stock	$	$ 3,000

See notes to consolidated financial statements.

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CAPITAL PROPERTIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SIX MONTHS ENDED JUNE 30, 2010 AND 2009
(Unaudited)

1. Description of business:

Capital Properties, Inc. and its wholly-owned subsidiaries, Tri-State Displays, Inc., Capital Terminal Company and Dunellen, LLC (collectively referred to as the Company), operate in two segments: (1) Leasing and (2) Petroleum Storage.

The leasing segment consists of the long-term leasing of certain of its real estate interests in downtown Providence, Rhode Island (upon the commencement of which the tenants are required to construct buildings thereon, with the exception of a parking garage), the leasing of a portion of its building (Steeple Street Building) under short-term leasing arrangements and the leasing of locations along interstate and primary highways in Rhode Island and Massachusetts to Lamar Outdoor Advertising, LLC (Lamar) which has constructed outdoor advertising boards thereon. The Company anticipates that the future development of its remaining properties in and adjacent to the Capital Center area will consist primarily of long-term ground leases. Pending this development, the Company leases these parcels for public parking under short-term leasing arrangements to Metropark, Ltd. (Metropark).

The petroleum storage segment consists of operating the petroleum storage terminal (the Terminal) and the Wilkesbarre Pier (the Pier), collectively referred to as the Facility, located in East Providence, Rhode Island, for Global Companies, LLC (Global) which stores and distributes petroleum products.

The principal difference between the two segments relates to the nature of the operations. In the leasing segment, the tenants under long-term land leases incur substantially all of the development and operating costs of the assets constructed on the Company s land, including the payment of real property taxes on both the land and any improvements constructed thereon; whereas the Company is responsible for the operating and maintenance expenditures, including a portion of the real property taxes, as well as capital improvements at the Facility.

2. Principles of consolidation and basis of presentation:

The accompanying condensed consolidated financial statements include the accounts and transactions of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying condensed consolidated balance sheet as of December 31, 2009, has been derived from audited financial statements and the unaudited interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to those rules and regulations, although the Company believes that the disclosures made are adequate to make the information not misleading. It is suggested that these condensed financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in the Company s latest Form 10-K. In the opinion of management, the accompanying condensed consolidated financial statements contain all adjustments (consisting solely of normal recurring adjustments) necessary to present fairly the financial position as of June 30, 2010, the results of operations for the three and six months ended June 30, 2010 and 2009, and cash flows for the six months ended June 30, 2010 and 2009.

The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year.

New accounting standards:

The Company reviews new accounting standards as issued. Although some of these accounting standards may be applicable to the Company, the Company has not identified any standards that it believes merit further discussion. The Company expects that none of the new standards would have a significant impact on its consolidated financial statements.

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3. Use of estimates:

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

4. Properties and equipment:

Properties and equipment consists of the following:

	June 30, 2010	December 31, 2009
Properties on lease or held for lease:		
Land and land improvements	$ 4,621,000	$ 4,621,000
Building and improvements, Steeple Street	1,961,000	1,772,000
Construction in progress	2,633,000	2,246,000
	9,215,000	8,639,000
Petroleum storage facility, on lease:		
Land and land improvements	5,591,000	5,591,000
Buildings and structures	1,748,000	1,744,000
Tanks and equipment	14,600,000	14,600,000
	21,939,000	21,935,000
Office equipment	131,000	131,000
	31,285,000	30,705,000
Less accumulated depreciation:		
Properties on lease or held for lease	151,000	104,000
Petroleum storage facility, on lease	8,754,000	8,430,000
Office equipment	106,000	102,000
	9,011,000	8,636,000
	$ 22,274,000	$ 22,069,000

In June 2009, the Company commenced the construction of the historic restoration and utility infrastructure of the Steeple Street Building at an original estimated cost of $2,100,000. In July 2010, the restoration was substantially completed at a total cost of $2,633,000 plus tenant improvements not originally budgeted of $189,000.

5. Note payable:

In April 2010**,** the Company borrowed $6,000,000 from a bank. The loan bears interest at the rate of 6 percent per annum and has a term of ten years with repayments on a twenty-year amortization schedule (monthly principal payments of $25,000 plus interest). The loan matures April 26, 2020 and contains the customary covenants, terms and conditions and permits prepayment, in whole or in part, at any time without penalty if the prepayment is made from internally generated funds. As collateral for the loan, the Company granted the bank a mortgage on Parcels 3S and 5 in the Capital Center.

In May 2010, the proceeds from the loan were used principally to fund a special dividend of $5,478,000 to shareholders, which represented the Company s earnings and profits as calculated for federal income tax purposes at December 31, 2009.

In connection with the borrowing, the Company incurred financing fees totaling $55,000, which are included in prepaid and other on the accompanying consolidated balance sheet at June 30, 2010. These fees are being amortized on a straight-line basis over the 10-year term of the note and are included in interest expense on the accompanying consolidated statements of income for the three and six months ended June 30, 2010.

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6. Description of leasing arrangements:

Long-term land leases:

As of June 30, 2010, the Company had entered into six long-term land leases for six separate parcels upon which the improvements have been completed (developed parcels). In addition, in 2005 a long-term land lease commenced on an undeveloped parcel on which two residential buildings were planned. One building was completed in September 2009. The other building has not progressed beyond the early stages of site preparation and the timing of its construction and completion is uncertain.

Under the seven land leases, the tenants are required to negotiate any tax stabilization treaty or other arrangements, appeal any changes in real property assessments, and pay real property taxes assessed under these arrangements. Accordingly, the amounts payable by the tenants are excluded from leasing revenues and leasing expenses on the accompanying consolidated statements of income. The real property taxes attributable to the Company s land under these leases totaled $250,000 and $500,000, respectively, for the three and six months ended June 30, 2010, and $360,000 and $720,000, respectively, for the three and six months ended June 30, 2009.

Under the lease which commenced in 2005, the tenant is entitled to a credit for future rents equal to a portion of the real property taxes paid by the tenant through April 2007, which credit totaled $520,000 at June 30, 2010. In connection with Phase I of the tenant s project, commencing July 1, 2010, the annual rent increased from $48,000 to $300,000. As a result of the rent credit, the tenant will not be required to make cash payments for rent for the next 21 months. Each month during the period of the rent credit, the Company will reclassify $25,000 of deferred leasing revenues to leasing revenues.

Short-term leases:

The Company leases the undeveloped parcels of land in or adjacent to the Capital Center area for public parking purposes to Metropark, Ltd. under a short-term cancellable lease.

A former tenant of the Steeple Street Building filed for receivership in November 2009. At December 31, 2009, the former tenant owed the Company $40,000 and the Company recorded an allowance for doubtful accounts of $40,000. At March 31, 2010, the former tenant owed the Company an additional $22,000 and the Company recorded an allowance for doubtful accounts for the additional amount. In June 2010, the former tenant sold its operations to a new tenant who assumed the lease and paid the Company in full; the Company has reversed the allowance for doubtful accounts for the full amount.

At June 30, 2010, the Company has two tenants in a portion of the Steeple Street Building (including the new tenant who assumed the lease) under short-term leases (five years or less) at a current annual rental of $114,000. The Company is seeking additional tenants for the remaining available space.

7. Petroleum storage facility:

Environmental remediation:

In 1994, a leak was discovered in a 25,000 barrel storage tank at the Terminal which allowed the escape of a small amount of fuel oil. All required notices were made to the State of Rhode Island Department of Environmental Management (RIDEM). In 2000, the tank was demolished and testing of the groundwater indicated that there was no large pooling of contaminants. In 2001, RIDEM approved a plan pursuant to which the Company installed a passive system consisting of three wells and commenced monitoring the wells.

In 2003, RIDEM decided that the passive monitoring system previously approved was not sufficient and required the Company to design an active remediation system for the removal of product from the contaminated site. The Company and its consulting engineers began the pre-design testing of the site in the fourth quarter of 2004. The consulting engineers estimated a total cost of $200,000 to design, install and operate the system, which amount was accrued in 2004. Through 2006, the Company had expended $119,000 and has not incurred any additional costs since then. RIDEM has not taken any action on the Company s proposed plan. As designed, the system will pump out the contaminants which will be disposed of in compliance with applicable regulations. After a period of time, the groundwater will be tested to determine if sufficient contaminants have been removed. While the Company and its consulting engineers believe that the proposed active remediation system will correct the situation, it is possible that RIDEM could require the Company to expand remediation efforts, which could result in the Company incurring additional costs.

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Environmental incident:

In 2002, during testing of monitoring wells at the Terminal, the Company s consulting engineer discovered free floating phase product in a groundwater monitoring well located on that portion of the Terminal purchased in 2000. Laboratory analysis indicated that the product was gasoline, which is not a product the Company ever stored at the Terminal. The Company commenced an environmental investigation and analysis, the results of which indicate that the gasoline did not come from the Terminal. The Company notified RIDEM. RIDEM subsequently identified Power Test Realty Partnership (Power Test), the owner of an adjacent parcel, as a potentially responsible party for the contamination. Getty Properties Corp. is the general partner of Power Test. Power Test challenged that determination and, after an administrative hearing, on October 20, 2008, a RIDEM Hearing Officer determined that Power Test is responsible for the discharge of the petroleum product under the Rhode Island Oil Pollution Control Act, R.I.G.L. Section 46-12.5.1-3 and Rule 6(a) and 12(b) of the Oil Pollution Control Regulations. The RIDEM Decision and Order requires Power Test to remediate the contamination as directed by RIDEM. In November 2008, Power Test appealed the decision to the Rhode Island Superior Court. In addition, in November 2008, Power Test sought, and received, a stay of the Decision and Order of the Hearing Officer pending a clarification by RIDEM of the amount of the proposed fine. There can be no assurance that the Superior Court will affirm the decision of the Administrative Hearing Officer.

In April 2009, the Company sued Power Test and Getty Properties Corp. in the Rhode Island Superior Court seeking remediation of the site or, in the alternative, the cost of the remediation. On May 1, 2009, Power Test and Getty Properties Corp. removed the action to the United States District Court for the District of Rhode Island. On May 22, 2009, Power Test and Getty Properties Corp. answered the Complaint and filed a Counterclaim against Dunellen, LLC and Capital Terminal Company alleging that Dunellen, LLC and Capital Terminal Company are responsible for the contamination. Getty Properties Corp. and Power Test have joined Getty Petroleum Marketing, Inc., the tenant under a long-term lease with Getty Properties Corp. of the adjacent property, as a defendant. The parties are now engaged in discovery. There can be no assurance that the Company will prevail in this litigation.

Since January 2003, the Company has not incurred significant costs in connection with this matter, other than ongoing litigation costs, and is unable to determine the costs it might incur to remedy the situation, as well as any costs to investigate, defend and seek reimbursement from the responsible party with respect to this contamination.

8. Income taxes:

The income tax provision for the three and six months ended June 30, 2010, does not bear the customary relationship between tax expense and pretax accounting income. The Company has determined that the expenditures in connection with the historic restoration of the Steeple Street Building qualify for federal historic income tax credits in 2010 of approximately $500,000 and has incorporated the credit in determining the effective tax rate for 2010 in the accompanying consolidated financial statements.

9. Operating segment disclosures:

The Company operates in two segments: (1) Leasing and (2) Petroleum Storage.

The Company makes decisions relative to the allocation of resources and evaluates performance based on each segment s respective income before income taxes, excluding interest income and expense, and certain corporate expenses.

Inter-segment revenues are immaterial in amount. The Company incurred interest expense of $64,000 for the six months ended June 30, 2010. The Company did not incur interest expense during the six months ended June 30, 2009.

The following financial information is used for making operating decisions and assessing performance of each of the Company s segments for the six months ended June 30, 2010 and 2009:

	2010	2009

Leasing:		
Revenues:		
Long-term leases:		
Contractual	$ 1,094,000	$ 1,053,000
Contingent	80,000	86,000
Short-term leases	316,000	335,000
Total revenues	$ 1,490,000	$ 1,474,000

	2010	2009
Property tax expense	$ 248,000	$ 245,000
Depreciation	$ 47,000	$ 21,000
Income before income taxes	$ 926,000	$ 1,067,000
Assets	$ 9,300,000	$ 6,895,000
Properties and equipment, additions	$ 576,000	$ 335,000
Petroleum storage:		
Revenues:		
Contractual	$ 1,889,000	$ 1,883,000
Contingent		2,000
Total revenues	$ 1,889,000	$ 1,885,000
Property tax expense	$ 117,000	$ 106,000
Depreciation	$ 324,000	$ 322,000
Income before income taxes	$ 758,000	$ 661,000
Assets	$ 13,604,000	$ 14,133,000
Properties and equipment, additions	$ 4,000	$ 67,000

The following is a reconciliation of the segment information to the amounts reported in the accompanying consolidated financial statements for the six months ended June 30, 2010 and 2009:

	2010	2009
Revenues for operating segments:		
Leasing	$ 1,490,000	$ 1,474,000
Petroleum storage	1,889,000	1,885,000
Total consolidated revenues	$ 3,379,000	$ 3,359,000

Property tax expense:		
Property tax expense for operating segments:		
Leasing	$ 248,000	$ 245,000
Petroleum storage	117,000	106,000
	365,000	351,000
Unallocated corporate property tax expense	2,000	2,000
Total consolidated property tax expense	$ 367,000	$ 353,000
Depreciation:		
Depreciation for operating segments:		
Leasing	$ 47,000	$ 21,000
Petroleum storage segment:	324,000	322,000
	371,000	343,000
Unallocated corporate depreciation	4,000	3,000
Total consolidated depreciation	$ 375,000	$ 346,000
Income before income taxes:		
Income before income taxes for operating segments:		