

CAPITAL PROPERTIES INC /RI/
Form 10-Q
August 05, 2015
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2015

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 001-08499

CAPITAL PROPERTIES, INC.

(Exact name of registrant as specified in its charter)

Rhode Island
(State or other jurisdiction of
incorporation or organization)

05-0386287
(IRS Employer
Identification No.)

100 Dexter Road

East Providence, Rhode Island
(Address of principal executive offices)

02914
(Zip Code)

(401) 435-7171

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the 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 (Section 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

Edgar Filing: CAPITAL PROPERTIES INC /RI/ - Form 10-Q

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

Accelerated filer

Non-accelerated filer

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

As of June 30, 2015, the Company had 6,599,912 shares of Class A Common Stock outstanding.

Table of Contents

CAPITAL PROPERTIES, INC.

FORM 10-Q

FOR THE QUARTER ENDED JUNE 30, 2015

TABLE OF CONTENTS

	Page
<u>PART I FINANCIAL INFORMATION</u>	
Item 1. <u>Financial Statements</u>	3
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	13
Item 4. <u>Controls and Procedures</u>	17
<u>PART II OTHER INFORMATION</u>	
Item 6. <u>Exhibits</u>	18
<u>Signatures</u>	19
Exhibits 31	Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibits 32	Certifications Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Table of ContentsPART I**Item 1. Financial Statements****CAPITAL PROPERTIES, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

	June 30, 2015 (unaudited)	December 31, 2014
ASSETS		
Properties and equipment (net of accumulated depreciation)	\$ 19,681,000	\$ 19,789,000
Cash	2,755,000	2,927,000
Prepaid and other	662,000	653,000
	\$ 23,098,000	\$ 23,369,000
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities:		
Notes payable:		
Bank (\$288,000 due within one year)	\$ 1,709,000	\$ 2,852,000
Dividend notes	11,787,000	11,787,000
Accounts payable and accrued expenses:		
Property taxes	283,000	282,000
Environmental remediation	79,000	80,000
Other	283,000	261,000
Income taxes payable	60,000	13,000
Deferred income taxes, net	4,840,000	5,011,000
	19,041,000	20,286,000
Shareholders equity:		
Class A common stock, \$.01 par; authorized 10,000,000 shares; issued and outstanding 6,599,912 shares	66,000	66,000
Capital in excess of par	782,000	782,000
Retained earnings	3,209,000	2,235,000
	4,057,000	3,083,000
	\$ 23,098,000	\$ 23,369,000

See notes to consolidated financial statements.

Table of Contents**CAPITAL PROPERTIES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF INCOME****THREE AND SIX MONTHS ENDED JUNE 30, 2015 AND 2014****(Unaudited)**

	Three Months Ended June 30		Six Months Ended June 30	
	2015	2014	2015	2014
Revenues:				
Leasing	\$ 1,334,000	\$ 1,288,000	\$ 2,514,000	\$ 2,397,000
Petroleum storage facility	880,000	732,000	1,755,000	1,304,000
	2,214,000	2,020,000	4,269,000	3,701,000
Expenses:				
Leasing	221,000	201,000	446,000	427,000
Petroleum storage facility	621,000	643,000	1,304,000	1,480,000
General and administrative	253,000	243,000	573,000	539,000
Interest on notes:				
Bank loan	23,000	45,000	48,000	92,000
Dividend notes	147,000	147,000	295,000	295,000
	1,265,000	1,279,000	2,666,000	2,833,000
Income before income taxes	949,000	741,000	1,603,000	868,000
Income tax expense (benefit):				
Current	446,000	378,000	800,000	455,000
Deferred	(71,000)	(87,000)	(171,000)	(114,000)
	375,000	291,000	629,000	341,000
Net income	\$ 574,000	\$ 450,000	\$ 974,000	\$ 527,000
Basic income per common share based upon 6,599,912 shares outstanding	\$.09	\$.07	\$.15	\$.08

See notes to consolidated financial statements.

Table of Contents**CAPITAL PROPERTIES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS****SIX MONTHS ENDED JUNE 30, 2015 AND 2014****(Unaudited)**

	2015	2014
Cash flows from operating activities:		
Net income	\$ 974,000	\$ 527,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	436,000	430,000
Amortization of deferred costs	23,000	7,000
Deferred income taxes	(171,000)	(114,000)
Other, principally net changes in prepaids, accounts payable, accrued expenses and current income taxes	(61,000)	21,000
Net cash provided by operating activities	1,201,000	871,000
Cash flows from investing activities:		
Purchases of properties and equipment	(230,000)	(33,000)
Cash flows from financing activities:		
Principal payments on note payable, bank	(1,143,000)	(1,143,000)
Decrease in cash	(172,000)	(305,000)
Cash, beginning	2,927,000	3,305,000
Cash, ending	\$ 2,755,000	\$ 3,000,000
Supplemental disclosures:		
Cash paid for:		
Income taxes	\$ 753,000	\$ 105,000
Interest	\$ 339,000	\$ 384,000
Non-cash investing and financing activities, capital expenditures financed through accounts payable	\$ 98,000	\$

See notes to consolidated financial statements.

Table of Contents

CAPITAL PROPERTIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

THREE AND SIX MONTHS ENDED JUNE 30, 2015 AND 2014

(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, leasing and petroleum storage.

The leasing segment consists of (i) 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 and Parcels 6B and 6C), (ii) the leasing of a portion of its building (Steeple Street Building) under short-term leasing arrangements and (iii) 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) containing 1,004,000 shell barrels and the Wilkesbarre Pier (the Pier), both of which are owned by the Company and are collectively referred to as the Facility, located in East Providence, Rhode Island, for Sprague Operating Resources LLC (Sprague), a wholly-owned subsidiary of Sprague Resources LP, 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. In the petroleum storage segment, the Company is responsible for the operating and maintenance expenditures and real estate taxes up to \$290,000 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, 2014, 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 United States generally accepted accounting principles (GAAP) 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, 2015, the results of operations for the three and six months ended June 30, 2015 and 2014, and the cash flows for the six months ended June 30, 2015 and 2014.

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

Environmental incidents:

The Company accrues a liability when an environmental incident has occurred and the costs are estimable. The Company does not record a receivable for recoveries from third parties for environmental matters until it has determined that the amount of the collection is reasonably assured. The accrued liability is relieved when the Company pays the liability or a third party assumes the liability. Upon determination that collection is reasonably assured or a third party assumes the liability, the Company records the amount as a reduction of expense.

Table of Contents

The Company charges to expense those costs that do not extend the life, increase the capacity or improve the safety or efficiency of the property owned or used by the Company.

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 expects that none of the new standards will have a significant impact on its consolidated financial statements.

3. Use of estimates:

The preparation of consolidated financial statements in conformity with GAAP 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 consolidated financial statements. Estimates also affect the reported amounts of income 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, 2015	December 31, 2014
Properties on lease or held for lease:		
Land and land improvements	\$ 4,701,000	\$ 4,701,000
Building and improvements, Steeple Street	5,802,000	5,545,000
	10,503,000	10,246,000
Petroleum storage facility, on lease:		
Land and land improvements	5,577,000	5,569,000
Buildings and structures	1,867,000	1,867,000
Tanks and equipment	14,770,000	14,707,000
	22,214,000	22,143,000
Office equipment	112,000	112,000
	32,829,000	32,501,000
Less accumulated depreciation:		
Properties on lease or held for lease	1,107,000	1,000,000
Petroleum storage facility, on lease	11,957,000	11,631,000
Office equipment	84,000	81,000

13,148,000 12,712,000

\$ 19,681,000	\$ 19,789,000
---------------	---------------

5. Notes payable:*Bank loan:*

In December 2012, the Company and the Bank entered into an Amended and Restated Loan Agreement (Loan Agreement) pursuant to which the Company refinanced the \$2,700,000 remaining balance of the 2010 debt to the Bank and borrowed an additional \$3,025,000. Pursuant to the Loan Agreement, the Company amended and restated the then existing note to the Bank, the first mortgage on Parcels 3S and 5 and certain other loan agreements. For the first five years, the loan bears interest at the annual rate of 3.34% and thereafter will bear interest on either a floating rate basis at LIBOR plus 215 basis points with a floor of 3.25% or a fixed rate of 225 basis points over the five-year Federal Home Loan Bank of Boston Classic Advance Rate (3.34% at June 30, 2015). The loan has a term of ten years with repayments on a 20-year amortization schedule (monthly principal payments of \$24,000 plus interest) and had a balloon payment for the outstanding balance in December 2022.

In May 2015, the Company prepaid \$1,000,000. As a result of this prepayment, the balloon payment was eliminated and the loan will be fully paid in June 2021 based on making payments required under the existing amortization schedule. In June and December 2014, the Company prepaid \$1,000,000 and \$1,300,000, respectively.

The Loan Agreement requires the Company to maintain at the Bank unencumbered liquid assets (cash or marketable securities) of \$1,000,000 and contains other customary terms and conditions.

Table of Contents

Financing fees totaling \$71,000 are being amortized by the straight-line method over the 10-year term of the note (which approximates the effective interest rate method). Amortization of deferred financing fees is included in interest expense on the accompanying consolidated statements of income. At June 30, 2015 and December 31, 2014, unamortized deferred financing fees are \$54,000 and \$57,000, respectively, which are included in prepaid and other on the accompanying consolidated balance sheets.

Dividend notes:

In 2012, the Company issued \$11,787,000 in principal face amount of 5% dividend notes due December 26, 2022 (the Dividend Notes). The Dividend Notes are unsecured general obligations of the Company bearing interest at the annual rate of 5% payable semi-annually on June 15 and December 15 to note holders of record on June 1 and December 1 of each year. The Dividend Notes may be redeemed in whole or in part at any time and from time to time at the option of the Company. The Dividend Notes are subject to mandatory redemption in an amount equal to the Net Proceeds from the sale of any real property owned by the Company or any of its subsidiaries. Net Proceeds is defined as the gross cash received by the Company from any such sale reduced by the sum of (a) costs relating to the sale, (b) federal and state income taxes as a result of the sale, and (c) the amount used by the Company to pay in whole or in part financial institution debts secured by a mortgage of the Company s or any subsidiary s real property regardless of whether such mortgage encumbers the property sold. The Company has obligated itself not to grant any mortgages on any of its property located in the Capital Center District in Providence, Rhode Island, other than Parcels 3S and 5, and to cause its subsidiaries not to grant any such mortgages, in each case without the consent of the holders of two-thirds of the outstanding principal face amount of the Dividend Notes. The Dividend Notes contain other customary terms and conditions.

6. Description of leasing arrangements:*Long-term land leases:*

As of June 30, 2015, the Company had entered into nine long-term land leases. Of the nine parcels, seven have had improvements constructed thereon.

Under the nine land leases, the tenants are required to negotiate any tax stabilization treaties or other arrangements, appeal any changes in real property assessments, and pay real property taxes assessed on land and improvements under these arrangements. Accordingly, real property taxes 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 \$307,000 and \$615,000, respectively, for the three and six months ended June 30, 2015, and \$319,000 and \$644,000, respectively, for the three and six months ended June 30, 2014.

In 2012, the Company entered into three amended and restated leases, each for a portion of the original Parcel 6 (Parcels 6A, 6B and 6C). All three leases have an initial term of approximately 95 years with two renewal terms of fifty years each. With respect to the Parcel 6B and 6C leases, an affiliate of the leasehold mortgagee guaranteed the payment by the tenants of rent and real property taxes as well as certain other tenant monetary obligations for a two-year period which terminated May 18, 2014. Commencing May 18, 2014, each of the lessees of Parcels 6B and 6C has the right to terminate its lease at any time during the remaining term of that lease upon thirty days notice. To date, no notice of termination has been received by the Company. The current annual rent on Parcel B is \$194,000. On July 1, 2015, rent commenced on Parcel 6C at the annual rate of \$200,000.

Lamar lease:

The Company, through a wholly-owned subsidiary, leases 23 outdoor advertising locations containing 44 billboard faces along interstate and primary highways in Rhode Island and Massachusetts to Lamar under a lease which expires in 2045. The Lamar lease provides, among other things, for the following: (1) the base rent will increase annually at the rate of 2.75% for each leased billboard location on June 1 of each year, and (2) in addition to base rent, for each 12-month period commencing each June 1, Lamar must pay to the Company within thirty days after the close of the lease year 30% of the gross revenues from each standard billboard and 20% of the gross revenues from each electronic billboard for such 12-month period, reduced by the sum of (a) commissions paid to third parties and (b) base monthly rent for each leased billboard display for each 12-month period. For the lease years ended May 31, 2015 and 2014, the percentage rent totaled \$149,000 and \$173,000, respectively, which amounts are included in leasing revenues of the accompanying consolidated statements of income for the three and six months ended June 30, 2015 and 2014.

Table of Contents

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 under a short-term cancellable lease.

At June 30, 2015, the Company has three tenants occupying 65 percent of the Steeple Street Building under short-term leases of five years or less at a current annual rent of \$140,000. The Company is recognizing the revenue from these leases on a straight-line basis over the terms of the leases. At June 30, 2015 and December 31, 2014, the excess of straight-line over contractual rentals is \$4,000 and \$6,000, respectively, which is included in prepaid and other on the accompanying consolidated balance sheets. The Company also reports as revenue from tenants reimbursements for common area costs and real property taxes. On July 1, 2015, the Company leased an additional 10 percent of the building to a new tenant under a five-year lease at an annual rent of \$21,000. The Company is currently marketing for lease the remaining unoccupied portions of the building.

7. Petroleum storage facility and environmental incidents:

Leasing of the Facility:

For the first four months of 2014, the Company leased a portion of the Facility (425,000 shell barrels) to Atlantic Trading & Marketing, Inc. (ATMI) who vacated the Facility on April 30, 2014.

Effective May 1, 2014, the Company entered into a Petroleum Storage Services Agreement (the Agreement) with Sprague Operating Resources, LLC (Sprague) for the lease of its entire storage capacity of 1,004,000 barrels for a term of five years. The base rent is \$3,500,000, subject to annual cost-of-living adjustments on May 1 of each year. There was no change in the base rent on May 1, 2015 because the cost-of-living decreased from May 1, 2014. In addition, the Company will receive an additional \$.15 for each barrel of throughput at the facility in excess of 3,500,000 barrels in any contract year (May 1 to April 30). The total throughput for the year ending April 30, 2015 did not exceed 3,500,000 barrels. Sprague has the right to extend the Agreement for two additional terms of five years each, provided that Sprague gives at least twelve months notice prior to the expiration of the initial or the extension term, as applicable. Commencing April 1, 2016 and on each April 1 thereafter during the initial term and any extension term, either party during the following thirty days has the right to terminate the Agreement as of April 30 of the year next following the year in which notice of termination is given.

Commencing May 1, 2015, Sprague is obligated to reimburse the Company for any real property taxes in excess of \$290,000. There was no increase in the assessment or tax rate for the year 2015 and therefore no additional payment was due from Sprague.

The Company incurred \$108,000 in fees in connection with the execution of the Agreement, which amounts are being amortized on the straight-line method over the three-year non-cancellable portion of the term of the Agreement and are included in petroleum storage facility expenses on the accompanying consolidated statements of income for the three and six months ended June 30, 2015. At June 30, 2015 and December 31, 2014, unamortized deferred agreement costs were \$64,000 and \$84,000, respectively, which are included in prepaid and other on the accompanying consolidated balance sheets.

Wilkesbarre Pier:

The Pier is a deep-water pier in East Providence, Rhode Island owned by the Company which is integral to the operation of the Terminal. The Pier and the Terminal are connected by two petroleum pipelines which the Company

has a permanent right to use.

Environmental incident (2002):

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 the Rhode Island Department of Environmental Management (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, in October 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

Table of Contents

as directed by RIDEM and remanded the proposed penalty to RIDEM for recalculation. 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 penalty. In October 2009, RIDEM issued a recalculated administrative penalty, and, subsequently, the RIDEM Hearing Officer issued a recommended amended decision, which was affirmed as a final decision by the RIDEM Director in December 2009. In January 2010, Power Test appealed that decision to the Superior Court. In September 2011, the Superior Court affirmed the decision of the RIDEM director. Power Test has appealed that decision to the Rhode Island Supreme Court. The Supreme Court has not decided the appeal.

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 (the Court). 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 joined Getty Petroleum Marketing, Inc., the tenant under a long-term lease with Getty Properties Corp. of the adjacent property, as a defendant. The Company amended its Complaint to add Getty Petroleum Marketing, Inc. as a defendant. Getty Petroleum Marketing, Inc. moved for summary judgment against the Company, Getty Properties Corp. and Power Test. On December 5, 2011, Getty Petroleum Marketing, Inc. filed for bankruptcy under Chapter 11 of the United States Bankruptcy Act. Thereafter, with Bankruptcy Court approval, Getty Petroleum Marketing, Inc. rejected its lease with Getty Properties Corp. On August 24, 2012, the Bankruptcy Court approved a plan to liquidate Getty Petroleum Marketing, Inc. On January 15, 2013, the Court granted Getty Petroleum Marketing, Inc. s motion for summary judgment against the Company, Getty Properties Corp. and Power Test, dismissing the Company s third-party complaint.

The parties have agreed to stay the litigation pending a determination by the Rhode Island Supreme Court on the Power Test appeal.

There can be no assurance that the Company will prevail in this litigation.

Since 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.

Environmental remediation (1994):

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 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 significant costs since then. In 2011, RIDEM notified the company to proceed with the next phase of the approval process, notifying the abutters of the proposed remediation system even though RIDEM has not yet 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. In 2014, the Company engaged new consultants to work with RIDEM to develop the next phase of the approval process. 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 costs in excess of the remaining accrual of \$79,000.

Table of Contents**8. Income taxes:**

Deferred income taxes are recorded based upon differences between financial statement and tax basis amounts of assets and liabilities. The tax effects of temporary differences which give rise to deferred tax assets and liabilities were as follows:

	June 30, 2015	December 31, 2014
Gross deferred tax liabilities:		
Property having a financial statement basis in excess of tax basis	\$ 4,890,000	\$ 5,016,000
Insurance premiums and accrued leasing revenues	83,000	143,000
	4,973,000	5,159,000
Deferred tax assets	(133,000)	(148,000)
	\$ 4,840,000	\$ 5,011,000

9. Operating segment disclosures:

The Company operates in two segments, leasing and 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 expense and certain corporate expenses.

Inter-segment revenues are immaterial in amount.

The following financial information is used for making operating decisions and assessing performance of each of the Company's segments for the three and six months ended June 30, 2015 and 2014:

	Three Months Ended June 30		Six Months Ended June 30	
	2015	2014	2015	2014
Leasing:				
Revenues:				
Long-term land leases:				
Contractual	\$ 940,000	\$ 878,000	\$ 1,875,000	\$ 1,753,000
Contingent	175,000	200,000	200,000	225,000
Short-term leases	219,000	210,000	439,000	419,000
Total revenues	\$ 1,334,000	\$ 1,288,000	\$ 2,514,000	\$ 2,397,000
Property tax expense	\$ 102,000	\$ 100,000	\$ 210,000	\$ 210,000

Edgar Filing: CAPITAL PROPERTIES INC /RI/ - Form 10-Q

Depreciation	\$ 53,000	\$ 54,000	\$ 107,000	\$ 107,000
Income before income taxes	\$ 1,113,000	\$ 1,087,000	\$ 2,068,000	\$ 1,970,000
Assets	\$ 9,810,000	\$ 9,825,000	\$ 9,810,000	\$ 9,825,000
Properties and equipment, additions	\$ 257,000	\$	\$ 257,000	\$
<i>Petroleum storage:</i>				
Revenues, contractual	\$ 880,000	\$ 732,000	\$ 1,755,000	\$ 1,304,000
Property tax expense	\$ 69,000	\$ 70,000	\$ 144,000	\$ 145,000
Depreciation	\$ 164,000	\$ 161,000	\$ 326,000	\$ 322,000
Income (loss) before income taxes	\$ 259,000	\$ 89,000	\$ 451,000	\$ (176,000)
Assets	\$ 10,960,000	\$ 11,354,000	\$ 10,960,000	\$ 11,354,000
Properties and equipment, additions	\$ 71,000	\$ 33,000	\$ 71,000	\$ 33,000

Table of Contents

The following is a reconciliation of the segment information to the amounts reported in the accompanying consolidated financial statements for the three and six months ended June 30, 2015 and 2014:

	Three Months Ended June 30		Six Months Ended June 30	
	2015	2014	2015	2014
Revenues for operating segments:				
Leasing	\$ 1,334,000	\$ 1,288,000	\$ 2,514,000	\$ 2,397,000
Petroleum storage	880,000	732,000	1,755,000	1,304,000
Total consolidated revenues	\$ 2,214,000	\$ 2,020,000	\$ 4,269,000	\$ 3,701,000
Property tax expense:				
Property tax expense for operating segments:				
Leasing	\$ 102,000	\$ 100,000	\$ 210,000	\$ 210,000
Petroleum storage	69,000	70,000	144,000	145,000
	171,000	170,000	354,000	355,000
Unallocated corporate property tax expense	1,000	1,000	2,000	2,000
Total consolidated property tax expense	\$ 172,000	\$ 171,000	\$ 356,000	\$ 357,000
Depreciation:				
Depreciation for operating segments:				
Leasing	\$ 53,000	\$ 54,000	\$ 107,000	\$ 107,000
Petroleum storage segment:	164,000	161,000	326,000	322,000
	217,000	215,000	433,000	429,000
Unallocated corporate depreciation	1,000		3,000	1,000
Total consolidated depreciation	\$ 218,000	\$ 215,000	\$ 436,000	\$ 430,000
Income (loss) before income taxes:				
Income (loss) before income taxes for operating segments:				
Leasing	\$ 1,113,000	\$ 1,087,000	\$ 2,068,000	\$ 1,970,000
Petroleum storage	259,000	89,000	451,000	(176,000)
	1,372,000	1,176,000	2,519,000	1,794,000
Unallocated corporate expenses	(253,000)	(243,000)	(573,000)	(539,000)
Interest expense	(170,000)	(192,000)	(343,000)	(387,000)

Edgar Filing: CAPITAL PROPERTIES INC /RI/ - Form 10-Q

Total consolidated income before income taxes	\$ 949,000	\$ 741,000	\$ 1,603,000	\$ 868,000
---	------------	------------	--------------	------------

Assets:

Assets for operating segments:

Leasing	\$ 9,810,000	\$ 9,825,000	\$ 9,810,000	\$ 9,825,000
Petroleum storage	10,960,000	11,354,000	10,960,000	11,354,000

	20,770,000	21,179,000	20,770,000	21,179,000
--	------------	------------	------------	------------

Corporate cash	2,299,000	2,688,000	2,299,000	2,688,000
----------------	-----------	-----------	-----------	-----------

Other unallocated amounts	29,000	32,000	29,000	32,000
---------------------------	--------	--------	--------	--------

Total consolidated assets	\$ 23,098,000	\$ 23,899,000	\$ 23,098,000	\$ 23,899,000
---------------------------	---------------	---------------	---------------	---------------

Properties and equipment:

Additions to properties and equipment for operating segments:

Leasing	\$ 257,000	\$ 33,000	\$ 257,000	\$ 33,000
Petroleum storage	71,000	33,000	71,000	33,000

Total consolidated additions	\$ 328,000	\$ 33,000	\$ 328,000	\$ 33,000
------------------------------	------------	-----------	------------	-----------

10. Fair value of financial instruments:

The Company believes that the fair values of its financial instruments, including cash, receivables and payables, approximate their respective book values because of their short-term nature. The fair value of the bank note payable approximates its book value and was determined using borrowing rates currently available to the Company for loans with similar terms and maturities. The fair value of the dividend notes payable approximates their book value. The fair values described herein were determined using significant other observable inputs (Level 2) as defined by GAAP, which included statistics for the issuance, rating and trading of corporate debt securities issued by other companies.

Table of Contents

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations
FORWARD LOOKING STATEMENTS

Certain portions of this report, and particularly the Management's Discussion and Analysis of Financial Condition and Results of Operations, contain forward-looking statements within the meaning of Sections 27A of the Securities Act of 1933, as amended, and Sections 21E of the Securities Exchange Act of 1934, as amended, which represent the Company's expectations or beliefs concerning future events. The Company cautions that these statements are further qualified by important factors that could cause actual results to differ materially from those in the forward-looking statements, including, without limitation, the following: the ability of the Company to generate adequate amounts of cash; the collectability of the accrued leasing revenues when due over the terms of the long-term land leases and the early termination of the Parcel 6B and Parcel 6C land leases; the commencement of additional long-term land leases; changes in economic conditions that may affect either the current or future development on the Company's parcels; the right of the petroleum storage facility tenant to terminate the lease of the Facility effective April 30, 2017 and each April 30th thereafter; and exposure to contamination, remediation or similar costs associated with the operation of the petroleum storage facility. The Company does not undertake the obligation to update forward-looking statements in response to new information, future events or otherwise.

1. Overview:

Critical accounting policies:

The Company believes that its revenue recognition policy for long-term leases with scheduled rent increases (leasing segment) meets the definition of a critical accounting policy which is discussed in the Company's Form 10-K for the year ended December 31, 2014. There have been no changes to the application of this accounting policy since December 31, 2014.

Segments:

The Company operates in two segments, leasing and petroleum storage.

The leasing segment consists of (i) the long-term leasing of certain of its real estate interests in downtown Providence, Rhode Island (upon the commencement of which the tenants have been required to construct buildings thereon, with the exception of a parking garage and Parcels 6B and 6C), (ii) the leasing of a portion of the Steeple Street Building under short-term leasing arrangements and (iii) 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) containing 1,004,000 shell barrels and the Wilkesbarre Pier (the Pier), both of which are owned by the Company and are collectively referred to as the Facility, located in East Providence, Rhode Island, for Sprague Operating Resources LLC (Sprague), a wholly-owned subsidiary of Sprague Resources LP, 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. In the petroleum storage segment, the Company is responsible for the operating and maintenance expenditures and real estate taxes up to \$290,000 as well as capital improvements at the Facility.

Table of Contents**2. Liquidity and capital resources:***Bank loan:*

In December 2012, the Company and the Bank entered into an Amended and Restated Loan Agreement (*Loan Agreement*) pursuant to which the Company refinanced the \$2,700,000 remaining balance of the 2010 debt to the Bank and borrowed an additional \$3,025,000. Pursuant to the Loan Agreement, the Company amended and restated the then existing note to the Bank, the first mortgage on Parcels 3S and 5 and certain other loan agreements. For the first five years, the loan bears interest at the annual rate of 3.34% and thereafter will bear interest on either a floating rate basis at LIBOR plus 215 basis points with a floor of 3.25% or a fixed rate of 225 basis points over the five-year Federal Home Loan Bank of Boston Classic Advance Rate (3.34% at June 30, 2015). The loan has a term of ten years with repayments on a 20-year amortization schedule (monthly principal payments of \$24,000 plus interest) and had a balloon payment for the outstanding balance in December 2022.

In May 2015, the Company prepaid \$1,000,000. As a result of this prepayment, the balloon payment was eliminated and the loan will be fully paid in June 2021 based on making payments required under the existing amortization schedule. In June and December 2014, the Company prepaid \$1,000,000 and \$1,300,000, respectively.

The Loan Agreement requires the Company to maintain at the Bank unencumbered liquid assets (cash or marketable securities) of \$1,000,000 and contains other customary terms and conditions.

Dividend notes:

On December 7, 2012, the Board of Directors of the Company declared an extraordinary dividend of \$2.25 per share on its Class A and Class B common stock to shareholders of record on December 17, 2012. On December 27, 2012, the Company paid out \$3,063,000 in cash and issued \$11,787,000 in principal face amount of 5% dividend notes due December 26, 2022 (the *Dividend Notes*). The Dividend Notes are unsecured general obligations of the Company bearing interest at the annual rate of 5% payable semi-annually on June 15 and December 15 to note holders of record on June 1 and December 1 of each year. The Dividend Notes may be redeemed in whole or in part at any time and from time to time at the option of the Company. The Dividend Notes are subject to mandatory redemption in an amount equal to the Net Proceeds from the sale of any real property owned by the Company or any of its subsidiaries. Net Proceeds means the gross cash received by the Company from any such sale reduced by the sum of (a) costs relating to the sale, (b) federal and state income taxes as a result of the sale, and (c) the amount used by the Company to pay in whole or in part financial institution debts secured by a mortgage of the Company's or any subsidiary's real property regardless of whether such mortgage encumbers the property sold. The Company has obligated itself not to grant any mortgages on any of its property located in the Capitol Center District in Providence, Rhode Island, other than Parcels 3S and 5, and to cause its subsidiaries not to grant any such mortgages, in each case without the consent of the holders of two-thirds of the outstanding principal face amount of the Dividend Notes. The Dividend Notes contain other customary terms and conditions. The interest payments on an annual basis total \$589,000.

Petroleum storage facility:

For the first four months of 2014, the Company leased a portion of the Facility (425,000 shell barrels) to Atlantic Trading & Marketing, Inc. (*ATMI*) who vacated the Facility on April 30, 2014.

Effective May 1, 2014, the Company entered into a Petroleum Storage Services Agreement (*the Agreement*) with Sprague Operating Resources, LLC (*Sprague*) for the lease of its entire storage capacity of 1,004,000 barrels for a term of five years. The base rent is \$3,500,000, subject to annual cost-of-living adjustments on May 1 of each year.

There was no change in the base rent on May 1, 2015 because the cost-of-living decreased from May 1, 2014. In addition, the Company will receive an additional \$.15 for each barrel of throughput at the facility in excess of 3,500,000 barrels in any contract year (May 1 to April 30). The total throughput for the year ending April 30, 2015 did not exceed 3,500,000 barrels. Sprague has the right to extend the Agreement for two additional terms of five years each, provided that Sprague gives at least twelve months notice prior to the expiration of the initial or the extension term, as applicable. Commencing April 1, 2016 and on each April 1 thereafter during the initial term and any extension term, either party during the following thirty days has the right to terminate the Agreement as of April 30 of the year next following the year in which notice of termination is given.

Commencing May 1, 2015, Sprague is obligated to reimburse the Company for any real property taxes in excess of \$290,000. There was no increase in the assessment or tax rate for the year 2015 and therefore no additional payment was due from Sprague.

Table of Contents

During the first six months of 2015, the Company's operating activities provided \$1,201,000 of cash which was \$330,000 more than the cash provided by operating activities for the six months ended June 30, 2014. Cash and cash equivalents at June 30, 2015 decreased \$172,000 from year end. The increase in cash flows from operations and cash and cash equivalents was principally due to the commencement of the Sprague agreement on May 1, 2014 and scheduled increases in rentals under long-term land leases and increases under short-term leases.

Historically, the Company has had adequate liquidity to fund its operations.

Cash and cash commitments:

At June 30, 2015, the Company had cash of \$2,755,000. The Federal Deposit Insurance Corporation (FDIC) insures the Company's bank accounts to a maximum of \$250,000. The Company periodically evaluates the financial stability of the financial institution at which the Company's funds are held. In connection with the December 2012 Amended and Restated Loan Agreement, the Company is required to maintain unencumbered liquid assets (cash and marketable securities) of \$1,000,000 at the Bank.

Under the terms of two long-term land leases, the scheduled annual contractual rent increased in 2015 as follows: (1) on February 1, 2015, the rent on Parcel 8 increased \$20,000 and (2) on April 1, 2014, the rent on Parcel 7A increased \$9,000. On July 1, 2015, the rent commenced on Parcel 6C at the annual rate of \$200,000.

At June 30, 2015, the Company has three tenants occupying 65 percent of the Steeple Street Building under short-term leases (five years or less) at a current annual rental of \$140,000. On July 1, 2015, the Company leased an additional 10 percent of the building to a new tenant under a five-year lease at an annual rental of \$21,000. The Company is currently marketing for lease the remaining unoccupied portions of the building.

In May 2015, the Company prepaid \$1,000,000 on the bank loan payable. In June and December 2014, the Company prepaid \$1,000,000 and \$1,300,000, respectively, on the bank loan payable. Future prepayments will depend on the Company's level of available cash.

In light of the extraordinary dividend paid in December 2012, at each of the quarterly Board meetings held in 2014 and 2015, the Board of Directors voted to omit the regular quarterly dividend of \$0.03 per share. The Board will review the declaration of future dividends on a quarterly basis. The declaration of future dividends will depend on future earnings and financial performance.

3. Results of operations:**Three months ended June 30, 2015 compared to three months ended June 30, 2014:***Leasing segment:*

	2015	2014	Difference
Leasing revenues	\$ 1,334,000	\$ 1,288,000	\$ 46,000
Leasing expense	221,000	201,000	\$ 20,000
	\$ 1,113,000	\$ 1,087,000	

Leasing revenue increased due to scheduled increases in rentals under long-term land leases and increases under short-term leases, offset in part by a decrease in 2015 in the percentage rent under the Lamar lease. Leasing expense increased due to an increase in repairs and maintenance at the Steeple Street Building.

Petroleum storage segment:

	2015	2014	Difference
Petroleum storage facility revenues	\$ 880,000	\$ 732,000	\$ 148,000
Petroleum storage facility expense	621,000	643,000	\$ (22,000)
	\$ 259,000	\$ 89,000	

Petroleum storage facility revenues increased in 2015 due to Sprague leasing the entire Facility. Under a lease that terminated on April 30, 2014, the Company had leased to ATMI a portion of the storage capacity of the Facility. Petroleum storage facility expense decreased due to a decrease in insurance, offset in part by an increase in payroll and related costs.

Table of Contents*General:*

For the three months ended June 30, 2015, general and administrative expense increased \$10,000 due to an increase in payroll and related costs.

Interest expense:

For the three months ended June 30, 2015 and 2014, interest expense, bank loan is \$23,000 and \$45,000, respectively. In May 2015, the Company prepaid \$1,000,000 on the bank loan. In June and December 2014, the Company prepaid \$1,000,000 and \$1,300,000, respectively, on the bank loan. For the three months ended June 30, 2015 and 2014, interest expense, dividend notes remained at the same level.

Six months ended June 30, 2015 compared to six months ended June 30, 2014:*Leasing segment:*

	2015	2014	Difference
Leasing revenues	\$ 2,514,000	\$ 2,397,000	\$ 117,000
Leasing expense	446,000	427,000	\$ 19,000
	\$ 2,068,000	\$ 1,970,000	

Leasing revenue increased due to scheduled increases in rentals under long-term land leases and increases under short-term leases, offset in part by a decrease in 2015 in the percentage rent under the Lamar lease. Leasing expense increased due to an increase in repairs and maintenance at the Steeple Street Building.

Petroleum storage segment:

	2015	2014	Difference
Petroleum storage facility revenues	\$ 1,755,000	\$ 1,304,000	\$ 451,000
Petroleum storage facility expense	1,304,000	1,480,000	\$ (176,000)
	\$ 451,000	\$ (176,000)	

Petroleum storage facility revenues increased in 2015 due to Sprague leasing the entire Facility. Under a lease that terminated on April 30, 2014, the Company had leased to ATMI a portion of the storage capacity of the Facility. Petroleum storage facility expense decreased due to a decrease in repairs and maintenance, insurance and professional fees, offset in part by an increase in payroll and related costs.

General:

For the six months ended June 30, 2014, general and administrative expense increased \$34,000 due to an increase in payroll and related costs.

Interest expense:

For the six months ended June 30, 2015 and 2014, interest expense, bank loan is \$48,000 and \$92,000, respectively. In May 2015, the Company prepaid \$1,000,000 on the bank loan. In June and December 2014, the Company prepaid \$1,000,000 and \$1,300,000, respectively, on the bank loan. For the six months ended June 30, 2015 and 2014, interest expense, dividend notes remained at the same level.

Table of Contents

Item 4. Controls and Procedures

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the Exchange Act), the Company carried out an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. This evaluation was carried out under the supervision and with the participation of the Company's management, including the Company's principal executive officer and the Company's principal financial officer. Based upon that evaluation, the principal executive officer and the principal financial officer concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

There was no significant change in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that has materially affected, or is reasonably likely to affect, the Company's internal control over financial reporting. The Company continues to enhance its internal controls over financial reporting, primarily by evaluating and enhancing process and control documentation. Management discusses with and discloses these matters to the Audit Committee of the Board of Directors and the Company's auditors.

Table of Contents

PART II OTHER INFORMATION

Item 6. Exhibits

(b) Exhibits:

- 3.1** Restated Articles of Incorporation (incorporated by reference to Exhibit 3.1 to the registrant's report on Form 8-K filed on April 24, 2013).
- 3.2** By-laws, as amended (incorporated by reference to Exhibit 3.2 to the registrant's annual report on Form 10-K for the year ended December 31, 2007).
- 10** Material contracts:
 - Petroleum Storage Services Agreement between Sprague Operating Resources LLC and**
 - (a) Company:**
 - (i) Dated April 18, 2014 (incorporated by reference to Exhibit 10(a) to the registrant's Quarterly report on Form 10-Q for the quarter ended March 31, 2014)
 - (b) Amended Loan Agreement between Bank Rhode Island and Company:**
 - (i) Dated December 20, 2012 (incorporated by reference to Exhibit 10.1 to the registrant's report on Form 8-K filed on December 27, 2012)
 - (c) Form of Dividend Note:**
 - (i) Dated December 27, 2012 (incorporated by reference to Exhibit 10.2 to the registrant's report on Form 8-K filed on December 27, 2012)
 - (d) Lease between Metropark, Ltd. and Company:**
 - (i) Dated January 1, 2005 (incorporated by reference to Exhibit 10(a) to the registrant's annual report on Form 10-KSB for the year ended December 31, 2004), as amended.
- 31.1** Rule 13a-14(a) Certification of President and Principal Executive Officer
- 31.2** Rule 13a-14(a) Certification of Treasurer and Principal Financial Officer
- 32.1** Certification of President and Principal Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2** Certification of Treasurer and Principal Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101** The following financial information from the Company's Quarterly Report on Form 10-Q for the Quarter ended June 30, 2015, filed with the Securities and Exchange Commission on August 5, 2015, formatted in eXtensible Business Reporting Language:
 - (i) Consolidated Balance Sheets as of June 30, 2015 and December 31, 2014
 - (ii) Consolidated Statements of Income for the Three and Six Months ended June 30, 2015 and 2014
 - (iii) Consolidated Statements of Cash Flows for the Six Months ended June 30, 2015 and 2014
 - (iv) Notes to Consolidated Financial Statements.

Table of Contents

SIGNATURES

In accordance with the requirements of the Exchange Act, the Issuer caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CAPITAL PROPERTIES, INC.

By /s/ Robert H. Eder
Robert H. Eder

President and Principal Executive Officer

By /s/ Barbara J. Dreyer
Barbara J. Dreyer

Treasurer and Principal Financial Officer

DATED: August 5, 2015