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BNP RESIDENTIAL PROPERTIES INC
Form 10-Q
August 08, 2005

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2005

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: 1-9496

BNP RESIDENTIAL PROPERTIES, INC.
(Exact name of Registrant as specified in its charter)

Maryland

State or other jurisdiction of incorporation or organization

56-1574675

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

301 S. College Street, Suite 3850, Charlotte, NC 28202-6024
(Address of principal executive offices) (Zip Code)

704/944-0100
(Registrant's telephone number)

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 X No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes X No

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of July 29, 2005 (the latest practicable date).

| | |
|---|--|
| Common Stock, \$.01 par value ----- (Class) | 9,244,812 ----- (Number of shares) |
|---|--|

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PART I - Financial Information

Item 1. Financial Statements.

BNP RESIDENTIAL PROPERTIES, INC.

 Consolidated Balance Sheets - Unaudited
 (all amounts in thousands except share amounts)

| | June 30 2005 | Dece 2 |
|----------------------------------|-----------------|-----------|
| | ----- | |
| Assets | | |
| Real estate investments at cost: | | |
| Apartment properties | \$527,641 | |
| Restaurant properties | 37,405 | |
| | ----- | |
| | 565,047 | |
| Less accumulated depreciation | (80,120) | |
| | ----- | |
| | 484,927 | |
| Cash and cash equivalents | 2,533 | |

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| | |
|--|-----------|
| Prepaid expenses and other assets | 8,209 |
| Intangible assets, net | 1,251 |
| Deferred financing costs, net | 2,329 |
| | ----- |
| Total assets | \$499,250 |
| | ===== |
| Liabilities and Shareholders' Equity | |
| Deed of trust and other notes payable | \$410,480 |
| Accounts payable and accrued expenses | 3,700 |
| Accrued interest on notes payable | 1,721 |
| Consideration due for acquisitions | 1,000 |
| Deferred revenue and security deposits | 2,089 |
| | ----- |
| Total liabilities | 418,989 |
| Minority interest in consolidated limited partnerships | 274 |
| Minority interest in operating partnership | 19,637 |
| Shareholders' equity: | |
| Preferred stock, \$.01 par value, 10,000,000 shares authorized; issued and outstanding shares-- 909,090 at June 30, 2005, and December 31, 2004 | 10,000 |
| Common stock, \$.01 par value, 100,000,000 shares authorized; issued and outstanding shares-- 9,244,812 at June 30, 2005, 8,652,740 at December 31, 2004 | 92 |
| Additional paid-in capital | 112,012 |
| Dividend distributions in excess of net income | (61,754) |
| | ----- |
| Total shareholders' equity | 60,350 |
| | ----- |
| Total liabilities and shareholders' equity | \$499,250 |
| | ===== |

See accompanying notes

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BNP RESIDENTIAL PROPERTIES, INC.

 Consolidated Statements of Operations - Unaudited
 (all amounts in thousands except per share amounts)

| | Three months ended | | Six months e |
|--------------------------|--------------------|-----------|--------------|
| | June 30 | | June 30 |
| | 2005 | 2004 | 2005 |
| | ----- | | ----- |
| Revenues | | | |
| Apartment rental income | \$ 17,508 | \$ 10,579 | \$ 31,600 |
| Restaurant rental income | 957 | 957 | 1,915 |

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| | | | |
|--|-----------|---------|------------|
| Management fee income | 11 | 208 | 127 |
| Interest and other income | 26 | 113 | 251 |
| | 18,502 | 11,858 | 33,892 |
| Expenses | | | |
| Apartment operations | 6,853 | 4,388 | 12,296 |
| Apartment administration | 738 | 614 | 1,412 |
| Corporate administration | 637 | 561 | 1,522 |
| Interest and prepayment penalties | 5,728 | 3,330 | 10,818 |
| Depreciation | 4,157 | 2,690 | 7,678 |
| Amortization of deferred loan costs | 117 | 68 | 224 |
| Write-off of unamortized loan costs at debt refinance | 63 | - | 223 |
| Deficit distributions to minority partners | 800 | - | 7,621 |
| | 19,093 | 11,650 | 41,794 |
| (Loss) income before minority interests | (591) | 208 | (7,902) |
| Loss (income) attributed to minority interests - | | | |
| - Consolidated limited partnerships | 14 | - | 76 |
| - Operating partnership | 171 | 9 | 1,463 |
| Net (loss) income | (406) | 217 | (6,363) |
| Less cumulative preferred dividend | (250) | (250) | (500) |
| (Loss) income attributed to common shareholders | \$ (656) | \$ (33) | \$ (6,863) |
| Weighted average common shares outstanding | | | |
| | 9,239 | 7,119 | 9,111 |
| Earnings per common share - basic: | | | |
| Net (loss) income | \$ (0.04) | \$ 0.03 | \$ (0.70) |
| (Loss) income attributed to common shareholders | (0.06) | (0.01) | (0.75) |
| Earnings per common share - diluted: | | | |
| Net (loss) income | (0.04) | 0.02 | (0.70) |
| (Loss) income attributed to common shareholders | (0.06) | (0.01) | (0.75) |
| Dividends declared per common share | 0.25 | 0.25 | 0.50 |

See accompanying notes

BNP RESIDENTIAL PROPERTIES, INC.

Consolidated Statement of Shareholders' Equity - Unaudited
(all amounts in thousands)

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| | Preferred Stock | | Common Stock | | Additional | distribu |
|----------------------------|-----------------|-----------|--------------|--------|------------|----------|
| | Shares | Amount | Shares | Amount | paid-in | in exce |
| | | | | | capital | net in |
| Balance December 31, 2004 | 909 | \$ 10,000 | 8,653 | \$ 87 | \$ 103,221 | \$ (50 |
| Common stock issued | - | - | 580 | 6 | 8,596 | |
| Dividends paid - preferred | - | - | - | - | - | |
| Dividends paid - common | - | - | - | - | - | (2 |
| Net loss | - | - | - | - | - | (5 |
| Balance March 31, 2005 | 909 | 10,000 | 9,233 | 92 | 111,817 | (58 |
| Common stock issued | - | - | 12 | - | 194 | |
| Dividends paid - preferred | - | - | - | - | - | |
| Dividends paid - common | - | - | - | - | - | (2 |
| Net loss | - | - | - | - | - | |
| Balance June 30, 2005 | 909 | \$ 10,000 | 9,245 | \$ 92 | \$ 112,012 | \$ (61 |

See accompanying notes

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BNP RESIDENTIAL PROPERTIES, INC.

Consolidated Statements of Cash Flows - Unaudited
(all amounts in thousands)

| | Six months ended June 30 2005 |
|--|-------------------------------------|
| Operating activities: | |
| Apartment rental receipts, net | \$ 31,356 |
| Restaurant rental receipts | 1,915 |
| Management fee receipts | 127 |
| Interest and other income receipts | 269 |
| Operating and administrative expense payments | (15,812) |
| Interest payments | (10,806) |
| Net cash provided by operating activities | 7,048 |
| Investing activities: | |
| Acquisitions of apartment properties | (35,658) |
| Acquisition of Boddie Investment Company, net of cash included in accounts of consolidated limited partnerships | 193 |
| Additions to apartment properties, net | (4,097) |
| Net release (funding) of lender reserves | (2) |
| Net cash used in investing activities | (39,564) |
| Financing activities: | |
| Net proceeds from issuance of common stock | 1,082 |
| Distributions to minority partners in consolidated limited partnerships | (7,621) |

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| | |
|---|----------|
| Distributions to operating partnership minority unitholders | (916) |
| Dividends paid to preferred shareholder | (500) |
| Dividends paid to common shareholders | (4,580) |
| Proceeds from notes payable | 94,938 |
| Principal payments on notes payable | (46,908) |
| Payment of deferred financing costs | (962) |
| Net cash provided by financing activities | 34,532 |
| Net increase in cash and cash equivalents | 2,016 |
| Cash and cash equivalents at beginning of period | 517 |
| Cash and cash equivalents at end of period | \$ 2,533 |

(continued)

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BNP RESIDENTIAL PROPERTIES, INC.

Consolidated Statements of Cash Flows - Unaudited - continued
(all amounts in thousands)

| | Six months ended June 30 2005 |
|--|-------------------------------------|
| Reconciliation of net (loss) income to net cash provided by operating activities: | |
| Net (loss) income | \$ (6,363) |
| Amortization of intangible for in-place leases at acquisitions | 74 |
| Equity in income of unconsolidated limited partnership | - |
| Amortization of deferred interest defeasance | (77) |
| Depreciation and amortization of deferred loan costs | 7,902 |
| Write off of unamortized loan costs at debt refinancing | 223 |
| Deficit distributions to minority partners in consolidated limited partnerships | 7,621 |
| Minority interest in consolidated limited partnerships | (76) |
| Minority interest in operating partnership | (1,463) |
| Changes in operating assets and liabilities: | |
| Prepaid expenses and other assets | (2,931) |
| Accounts payable and accrued expenses | 2,396 |
| Deferred revenue, prepaid rent and security deposits | (259) |
| Net cash provided by operating activities | \$ 7,048 |

See accompanying notes

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BNP RESIDENTIAL PROPERTIES, INC.

Notes to Consolidated Financial Statements - June 30, 2005
(Unaudited)

Note 1. Interim financial statements

We prepared the accompanying condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. These interim financial statements do not include all information and notes required by generally accepted accounting principles for complete financial statements. However, except as disclosed herein, there has been no material change in the information disclosed in the notes to the consolidated financial statements included in the Annual Report on Form 10-K of BNP Residential Properties, Inc. for the year ended December 31, 2004. You should read these financial statements in conjunction with our 2004 Annual Report on Form 10-K. When we use the terms "company," "we," "us," or "our," we mean BNP Residential Properties, Inc. and all entities included in our consolidated financial statements. We believe that we have included all adjustments (including normal recurring accruals) necessary for a fair presentation. Operating results for the three and six months ending June 30, 2005, are not necessarily indicative of the results that may be expected for the year ending December 31, 2005.

We have reclassified certain amounts in our prior period consolidated financial statements and notes to conform to the current period presentation.

Note 2. Basis of presentation

The consolidated financial statements include the accounts of BNP Residential Properties, Inc. (the "company") and BNP Residential Properties Limited Partnership (the "operating partnership"). The company is the general partner and owns a majority interest in the operating partnership.

Effective January 26, 2005, in connection with an acquisition on that date, the consolidated financial statements also include the accounts of real estate limited partnerships (the "limited partnerships") that the operating partnership controls which are not considered variable interest entities ("VIEs"), as well as all VIEs for which the operating partnership is the primary beneficiary. The assets of consolidated limited partnerships controlled by the operating partnership generally are not available to pay creditors of the company or the operating partnership.

All significant intercompany balances and transactions have been eliminated in the consolidated financial statements.

Accounting for VIEs

In January 2003, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation 46, "Consolidation of Variable Interest Entities," ("FIN 46"). In December 2003, the FASB modified FIN 46 to make certain technical corrections and address certain implementation issues that had arisen. FIN 46 provided a new framework for identifying VIEs and determining when a company should include the assets, liabilities, noncontrolling interests and results of activities of a VIE in its consolidated financial statements.

In general, a VIE is an entity or other legal structure used to conduct activities or hold assets that either (1) has an insufficient amount of equity to carry out its principal activities without additional subordinated financial support, (2) has equity owners that, as a group, are unable to make significant decisions about its activities, or (3) has equity owners that, as a group, do not have the obligation to absorb losses or the right to receive returns generated by its operations.

FIN 46, as modified, requires a VIE to be consolidated if a party with an ownership, contractual or other financial interest in the VIE (a "variable interest holder") is obligated to absorb a majority of the risk of loss from the VIE's activities, is entitled to receive a majority of the VIE's residual returns (if no party absorbs a majority of the VIE's losses), or both. A variable interest holder that consolidates the VIE is called the "primary beneficiary." Upon consolidation, the primary beneficiary generally must initially record all of the VIE's assets, liabilities and noncontrolling interests at fair value and subsequently account for the VIE as if it were consolidated based on majority voting interest.

Accounting for general partner interests in limited partnerships

As managing general partner in three real estate limited partnerships, we have the ability to exercise significant influence over operating and financial policies. This influence is evident in the terms of the respective partnership agreements. However, under the guidance of the AICPA's Statement of Position 78-9 ("SOP 78-9"), we do not "control" the respective limited partnerships if the limited partners have significant rights, such as the right to replace the general partner and the right to approve the sale or refinancing of the assets of the respective partnership in accordance with the partnership agreement. In acting as the general partner in these limited partnerships, we are committed to providing additional levels of funding to meet partnership operating deficits as may be needed.

If we, as general partner, control a partnership that is not a VIE, generally accepted accounting principles require that we consolidate the partnership in our financial statements. Upon consolidation, we initially record our prorata interest in the partnership's assets and liabilities at the lower of our cost or fair value, and subsequently account for the partnership based on our prorata interest; the non-controlling interests are reflected in our financial statements at their historical costs.

Acquisition of interests in limited partnerships

Effective January 26, 2005, we acquired Boddie Investment Company ("BIC") in exchange for shares of our common stock valued at \$8.2 million. As a result of this acquisition, in addition to other significant assets, we acquired certain economic interests in the following limited partnerships:

- o Marina Shores Associates One, Limited Partnership - 50% interest as general partner
- o The Villages of Chapel Hill Limited Partnership - 1% interest as general partner
- o The Villages of Chapel Hill - Phase 5 Limited Partnership - 1% interest as general partner

Prior to this acquisition, we managed, on a fee basis, the properties owned by these limited partnerships. Following our acquisition of BIC, the operating partnership acts as the managing general partner of these limited partnerships and will continue to manage the properties. These limited partnerships are primarily funded with financing from third party lenders, which is secured by first deed of trust loans on the rental properties of the partnerships. The

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creditors of the limited partnerships generally do not have recourse to the operating partnership.

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We determined that the Marina Shores Associates One, Limited Partnership ("Marina Shores Partnership") is not a VIE. However, under the terms of the partnership agreement for the Marina Shores Partnership, the general partner controls the activities of the partnership; we have therefore included the accounts of this partnership in our consolidated financial statements effective January 26, 2005. The initial inclusion of the Marina Shores Partnership in our consolidated financial statements resulted in an increase in real estate investments of \$26.3 million, an increase in net operating assets of \$1.0 million and an increase in deed of trust notes payable of approximately \$21.4 million. Our initial net investment in this limited partnership was \$5.9 million.

We determined that The Villages of Chapel Hill Limited Partnership ("Villages Partnership") is a VIE, because the limited partnership does not have sufficient equity to carry out its principal activities without additional subordinated financial support from the general partner. We also determined that we are the primary beneficiary of the Villages Partnership. We have therefore included the accounts of this partnership in our consolidated financial statements effective January 26, 2005. The initial inclusion of the Villages Partnership in our consolidated financial statements resulted in an increase in real estate investments of \$14.2 million, an increase in net operating assets of \$0.1 million and an increase in deed of trust notes payable of approximately \$12.1 million. In addition, we hold approximately \$2.0 million in notes and other receivables from The Villages Partnership which has been eliminated in consolidation.

We determined that The Villages of Chapel Hill - Phase 5 Limited Partnership ("Villages - Phase 5 Partnership") is not a VIE. Following guidance in SOP 78-9, under the terms of the partnership agreement for the Villages - Phase 5 Partnership, the limited partners have certain voting rights that preclude control by the general partner. We have therefore accounted for our investment in this partnership by applying the equity method. Our initial investment in the Villages - Phase 5 Partnership was approximately \$7,000, and we include this investment in "other assets" on our balance sheet.

In late June 2005, the FASB ratified its Emerging Issues Task Force consensus in Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights" ("Issue 04-5"). This guidance states that the general partner in a limited partnership is presumed to control that limited partnership, with very limited exceptions. We have not yet made a final determination as to how the provisions of Issue 04-5 impact our accounting treatment for our interest in the Villages - Phase 5 Partnership. If applicable, we may be required to consolidate the accounts of the Villages - Phase 5 Partnership beginning no later than January 1, 2006; however, we do not expect that such a change in accounting treatment would have a material effect on our financial statements.

We reflect the unaffiliated partners' interests in the Marina Shores Partnership and the Villages Partnership as minority interest in consolidated limited partnerships. Minority interest in consolidated limited partnerships represents the minority partners' share of the underlying net assets of these consolidated limited partnerships. When these consolidated limited partnerships make cash distributions to partners in excess of the carrying amounts of the minority interests, we record a charge equal to the amount of such excess distributions as deficit distributions to minority partners. During the first quarter of 2005

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we recorded charges for deficit distributions to the minority partner in the Marina Shores Partnership totaling \$6.8 million. During the second quarter of 2005 we recorded additional charges for deficit distributions to the minority partner totaling \$0.8 million. There is no economic effect or cost to the company or the operating partnership for these distributions.

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We allocate proportional income and losses of the consolidated limited partnerships to minority partners to the extent of the carrying amount of the minority interest. We record a charge when losses attributable to the limited partners of a consolidated limited partnership exceed the carrying amount of the minority interest, even though there is no economic effect or cost to the operating partnership. In our initial consolidation of the Marina Shores Partnership, we reset the noncontrolling limited partner's capital account to \$-0-. During the first quarter of 2005, we recorded charges for consolidated limited partnership losses, resulting primarily from depreciation and costs related to refinance of the Marina Shores Partnership's first deed of trust loan, of approximately \$621,000 that were not allocated to the minority partner in Marina Shores Partnership because the losses exceeded the carrying amount of the minority interest. During the second quarter of 2005, we reduced these charges by \$203,000 for income that would otherwise have been allocated to the limited partner.

Stock-based compensation

The company has one employee Stock Option and Incentive Plan in place. As allowed by FAS 148, "Accounting for Stock-Based Compensation - Transition and Disclosure," and FAS 123 "Accounting for Stock-Based Compensation," we account for this plan using the intrinsic value method under the recognition and measurement principles of APB Opinion 25, "Accounting for Stock Issued to Employees," and related interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under this plan had an exercise price equal to the market value of the underlying common stock on the date of grant. All outstanding options were fully vested prior to the end of 2004. If we had applied the fair value recognition provisions of FAS 123 to this significant estimate for stock-based employee compensation, the effect would have been to reduce net income as reported by less than \$200 for the six months ended June 30, 2004, with no impact on net income as reported for the six months ended June 30, 2005, and no impact on basic and diluted earnings per share amounts as reported.

In December 2004 the Financial Accounting Standards Board issued FAS 123 (revised 2004), "Share Based Payment," ("FAS 123(R)") which is a revision of FAS 123. FAS 123(R) supersedes APB Opinion 25, and amends FAS 95, "Statement of Cash Flows." Generally, the approach in FAS 123(R) is similar to the approach described in FAS 123. However, FAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the statement of operations based on their fair values. Pro forma disclosure is no longer an alternative. FAS 123(R) must be adopted no later than January 1, 2006, and we expect to adopt FAS 123(R) as of that date.

Note 3. Apartment property acquisitions

During the first quarter of 2005, we completed the acquisition of a portfolio of four apartment properties from entities associated with Grover F. Shugart, Jr. and/or Brian D. Shugart, which we call the "Shugart Parties." The four properties contain an aggregate of 1,086 apartment units. The aggregate purchase price for the properties totaled \$52.1 million (including approximately \$0.3 million in net operating assets acquired), paid by the assumption or refinancing of \$42.8 million of debt on the properties and issuance of \$9.3 million in operating partnership units with an imputed value of \$13.50 per unit. Under the

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terms of the exchange agreements, we issued 689,000 operating partnership units at closing, and will issue an additional 74,000 deferred units in March 2006. The preliminary allocation of the purchase price includes the following significant components:

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| Property | Apt. Units | Contract Price | Debt Assumed | Val Oper Partne |
|------------------------------|---------------|----------------|--------------|-----------------------|
| | | (000's) | (000's) | (|
| Canterbury Apartments | 630 | \$ 25,750 | \$ 22,992 | \$ |
| Laurel Springs Apartments | 240 | 14,610 | 11,320 | |
| Laurel Springs II Apartments | 96 | 7,090 | 5,850 | |
| Salem Ridge Apartments | 120 | 4,360 | 2,610 | |

We will operate Laurel Springs and Laurel Springs II Apartments as one community.

During the second quarter of 2005, we completed two additional apartment property acquisitions in separate cash transactions. Both properties are located in the Charleston, South Carolina area.

| Property | Apt. Units | Contract Price |
|--------------------------|---------------|----------------|
| | | (000's) |
| Waverly Place Apartments | 240 | \$13,100 |
| Paces Watch Apartments | 232 | \$20,450 |

In addition, during the second quarter of 2005, we acquired approximately 40 acres of undeveloped land adjacent to our Canterbury Apartments property for a contract price of \$2.7 million, paid by \$0.6 million in cash and the assumption of \$2.1 million in debt which bears interest at the lender's prime rate and matures in September 2005.

Note 4. Financing transactions

Shortly after we acquired BIC (see Note 2 above) in January 2005, we completed the refinancing of debt related to the Marina Shores Partnership. The Marina Shores Partnership issued a \$33.9 million fixed-rate note payable, secured by a deed of trust and assignment of rents of Marina Shores Apartments. This loan provides for interest at 5.075% (5.145% effective rate), payable in monthly installments of principal and interest of \$184,000 through January 2015, with a balloon payment of \$28.2 million in February 2015. The Marina Shores Partnership first applied proceeds of this loan to retire the existing \$20.7 million deed of trust loan balance along with \$1.2 million interest and prepayment penalties, then distributed \$6.8 million to the minority limited partner and \$3.7 million to the operating partnership.

In conjunction with our acquisition of the four apartment properties from the Shugart Parties in March 2005, we assumed the following long-term debt:

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- o \$21.5 million balance, fixed-rate note payable, secured by a mortgage and assignment of rents of Canterbury Apartments. This loan provides for interest at 5.4% (5.48% effective rate), payable in monthly installments of principal and interest of \$124,000 through July 2013, with a balloon payment of \$18.4 million at maturity in August 2013.
- o \$1.5 million variable rate unsecured note related to Canterbury Apartments, which we immediately retired.

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- o \$11.3 million balance, fixed-rate note payable, secured by a deed of trust and assignment of rents of Laurel Springs Apartments. This loan provides for interest at 4.91% (4.98% effective rate), payable in monthly installments of principal and interest of \$62,000 through June 2013, with a balloon payment of \$9.6 million at maturity in July 2013.
- o \$5.9 million variable rate note payable, secured by a deed of trust and assignment of rents of Laurel Springs II Apartments. This loan provides for interest at 30-day LIBOR plus 1.9%, payable monthly. Beginning in June 2005, principal payments of \$7,000 will be due monthly in addition to interest, with a balloon payment of \$5.8 million at maturity in June 2006. At our option, we may extend the loan maturity to June 2008.
- o \$2.6 million fixed-rate note payable, secured by a deed of trust and assignment of rents of Salem Ridge Apartments. This loan provides for interest at 6.76%, payable in monthly installments of \$15,000 through September 2008, with principal due in full at that date.

In conjunction with our acquisitions during the second quarter of 2005, we issued the following debt:

- o \$10.2 million fixed-rate note payable, secured by a mortgage and assignment of rents of Waverly Place Apartments. This loan provides for interest at 5.31% (5.38% effective rate), with interest only monthly payments of \$46,000 through May 2008. Beginning June 2008, scheduled monthly installments of principal and interest will be \$56,000, with a balloon payment of \$9.1 million at maturity in June 2015.
- o \$14.9 million fixed-rate note payable, secured by a mortgage and assignment of rents of Paces Watch Apartments. This loan provides for interest at 5.31% (5.38% effective rate), with interest only monthly payments of \$67,000 through June 2008. Beginning July 2008, scheduled monthly installments of principal and interest will be \$83,000, with a balloon payment of \$13.3 million at maturity in June 2015.

Also, during the second quarter of 2005, we issued the following debt in refinancing transactions for two of our apartment properties:

- o \$15.5 million fixed-rate note payable, secured by a deed of trust and assignment of rents of Chason Ridge Apartments. This loan provides for interest at 5.21% (5.28% effective rate), with interest only monthly payments of \$68,000 through June 2008. Beginning July 2008, scheduled monthly installments of principal and interest will be \$85,000, with a balloon payment of \$13.9 million at maturity in June 2015.

We applied proceeds of this loan to retire an \$11.5 million variable-rate note payable. In conjunction with this retirement, we wrote off \$63,000 of unamortized loan costs.

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- o \$7.1 million fixed-rate note payable, secured by a deed of trust and assignment of rents of Harris Hill Apartments. This loan provides for interest at 5.21% (5.28% effective rate), with interest only monthly payments of \$31,000 through June 2008. Beginning July 2008, scheduled monthly installments of principal and interest will be \$39,000, with a balloon payment of \$6.4 million at maturity in June 2015.

We applied proceeds of this loan to retire an 8.55% fixed-rate note payable with a

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balance of \$5.5 million.

In conjunction with the various acquisition and financing transactions described above, we made net draws on our line of credit secured by Latitudes Apartments totaling \$5.0 million. In June 2005, we modified our line of credit secured by our 40 restaurant properties to extend the maturity date to January 2008.

Note 5. Shareholders' equity

In January 2005, we issued 508,578 shares of our common stock, valued at \$8.2 million, in conjunction with the BIC acquisition (see Note 2 above). As part of the acquisition, BIC surrendered, and we cancelled, 72,399 shares of our common stock, valued at \$1.2 million.

In February 2005, we issued 12,748 shares of our common stock through our Dividend Reinvestment and Stock Purchase Plan for proceeds of \$0.2 million. In May 2005, we issued 12,311 shares through this Plan for proceeds of \$0.2 million.

In March 2005, we issued 57,500 shares of our common stock upon exercise of options by two employees for proceeds of \$0.7 million.

Also in March 2005, we redeemed operating partnership units from a minority unitholder by issuing 73,333 shares of our common stock on a one-for-one basis.

We calculated basic and diluted earnings per common share using the following amounts (in thousands):

| | Three months ended June 30 | | Six months e June 30 |
|--|-------------------------------|---------|-------------------------|
| | 2005 | 2004 | 2005 |
| | (000's) | (000's) | (000's) |
| Numerators: | | | |
| Numerator for basic | | | |
| earnings per share - | | | |
| Net (loss) income | \$ (406) | \$ 217 | \$ (6,363) |
| Cumulative preferred dividend | (250) | (250) | (500) |
| | | | |
| (Loss) income attributed to common shareholders | \$ (656) | \$ (33) | \$ (6,863) |
| | | | |

Numerator for diluted

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| | | | |
|--|----------|---------|------------|
| earnings per share - | | | |
| Net (loss) income | \$ (406) | \$ 217 | \$ (6,363) |
| Loss (income) attributed to minority interest in operating partnership (1) | - | (9) | - |
| Cumulative preferred dividend | (250) | (250) | (500) |
| (Loss) income attributed to common shareholders | \$ (656) | \$ (42) | \$ (6,863) |

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| | Three months ended June 30 | | Six months e June 30 |
|---|-------------------------------|---------|-------------------------|
| | 2005 | 2004 | 2005 |
| | (000's) | (000's) | (000's) |
| Denominators: | | | |
| Denominator for basic earnings per share - weighted average common shares outstanding | 9,239 | 7,119 | 9,111 |
| Effect of dilutive securities: | | | |
| Convertible operating partnership units (1) | - | 1,850 | - |
| Stock options (2) | - | 24 | - |
| Denominator for diluted earnings per share - adjusted weighted average shares and assumed conversions | 9,239 | 8,994 | 9,111 |

- (1) Inclusion of operating partnership units would serve to reduce the net loss per share in calculation of 2005 amounts and have been excluded from the calculation.
- (2) We excluded options to purchase 60,000 shares of common stock at \$12.25, 120,000 shares of common stock at \$13.125, 60,000 shares of common stock at \$11.25, and 30,000 shares of common stock at \$9.25 from the calculation of diluted earnings per share for the three and six months ended June 30, 2005, because inclusion of these options would serve to reduce the net loss per share. We excluded options to purchase 120,000 shares of common stock at \$13.125 from the calculation of diluted earnings per share for the three and six months ended June 30, 2004; the exercise price of these options was greater than the average market price of the common shares for those periods, and the effect would be anti-dilutive.

Note 6. Subsequent events

The Board of Directors declared a regular quarterly dividend of \$0.25 per common share on July 21, 2005, payable on August 15, 2005, to shareholders of record as of August 1, 2005. The Board of Directors also authorized the payment of dividends totaling \$250,000 to the Series B Preferred shareholder.

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Effective August 1, 2005, the company and four members of senior management agreed to the terms upon which the company will enter into new employment agreements with each of the four officers. These terms provide for cash compensation and other benefits if we terminate them without cause or if a change in control of the company occurs. The Board of Directors also granted restricted stock awards for a total of 200,000 shares of common stock as of August 1, 2005, to the four officers. The shares vest annually at the rate of 10% per year, and carry all rights of ownership, including the receipt of dividends. The full terms of the restricted stock grants will be included in the employment agreements.

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

This Quarterly Report contains forward-looking statements within the meaning of federal securities law. You can identify such statements by the use of forward-looking terminology, such as "may," "will," "expect," "anticipate," "estimate," "continue" or other similar words. These statements discuss future expectations, contain projections of results of operations or of financial condition or state other "forward-looking" information.

Although we believe that our plans, intentions and expectations reflected in or suggested by these forward-looking statements are reasonable, we cannot assure you that we will achieve our plans, intentions or expectations. When you consider such forward-looking statements, you should keep in mind the following important factors that could cause our actual results to differ materially from those contained in any forward-looking statement:

- o Our markets could suffer unexpected increases in the development of apartment, other rental or competitive housing alternatives;
- o our markets could suffer unexpected declines in economic growth or an increase in unemployment rates;
- o general economic conditions could cause the financial condition of a large number of our tenants to deteriorate;
- o we may not be able to lease or re-lease apartments quickly or on as favorable terms as under existing leases;
- o we could incur unexpected costs in performing our third-party apartment property management activities;
- o we may have incorrectly assessed the environmental condition of our properties;
- o an unexpected increase in interest rates could cause our debt service costs to exceed expectations;
- o we may not be able to meet our long-term liquidity requirements on favorable terms; and
- o we could lose the services of key executive officers.

Given these uncertainties, we caution you not to place undue reliance on forward-looking statements. We undertake no obligation to disclose the results of any revision to these forward-looking statements we may make to reflect any future events or circumstances or to reflect the occurrence of unanticipated events.

You should read the discussion in conjunction with the financial statements and notes thereto included in this Quarterly Report and our Annual Report on Form 10-K.

Company Profile

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BNP Residential Properties, Inc. is a self-administered and self-managed real estate investment trust with operations in North Carolina, South Carolina and Virginia. Our primary activity is the ownership and operation of apartment communities. As of June 30, 2005, we owned and managed 33 apartment communities containing 8,384 units, including three communities containing 713 units for which we are the general partner of the entities that own the properties. In addition to our apartment communities, we own 40 properties that we lease on a triple-net basis to a restaurant operator.

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We are structured as an UpREIT, or umbrella partnership real estate investment trust. The company is the sole general partner and owns a controlling interest in BNP Residential Properties Limited Partnership, through which we conduct all of our operations. We refer to this partnership as the operating partnership. We refer to the limited partners of the operating partnership as minority unitholders or as the minority interest in the operating partnership.

Our executive offices are located at 301 South College Street, Suite 3850, Charlotte, North Carolina 28202-6024, telephone 704/944-0100.

Results of Operations

Summary

With good growth and comparisons, we were pleased with the results for the second quarter of 2005. Our focus during the second quarter was on increasing same-unit apartment revenue, which we were able to do with modest success. We entered the quarter with high occupancy at our apartment properties and knew that any increase in revenue would have to come as a result of increases in rental rates, not occupancy. During the quarter, continued strength in single-family home sales, fueled in large part by low home mortgage rates, made it difficult to increase rents as fast as we would have liked. Despite this, however, we were able to increase same-unit apartment rental income by 2.4%, all as the result of increases in rental rates.

We continue to be optimistic about the outlook for our properties, our markets and the company. We believe we will continue to see a slow strengthening in demand for the type of apartment property we operate and that we are well positioned to take advantage of this trend.

In January 2005, we acquired the general partner interest in three limited partnerships. The activities of two of these limited partnerships (and the apartment properties owned by those partnerships) are included in our consolidated financial statements as of January 26, 2005. We describe this acquisition in more detail under the heading "Capital Resources" as well as in the notes to our financial statements included in this Current Report on Form 10-Q.

Effective March 31, 2005, we acquired a portfolio of four apartment properties which we had previously managed under third-party contracts. (We will operate these as three apartment communities.) We subsequently acquired one apartment property effective April 21, 2005, and another property effective May 12, 2005. The activities of these owned properties have been included in our consolidated financial statements as of their respective acquisition dates.

Results of operations for the second quarter and first six months of 2005, compared to the same periods in 2004, reflect significant growth in our company and increased complexity in our financial reporting. We provide the following supplemental consolidating information, in response to requests from members of the investment community, for use in comparing our operating results

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for 2005 and 2004:

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| | 2005 | | | |
|--|--------------|---------|-------------------------|--------------------|
| | Consolidated | Elim | Consolidated LPs (1) | Owne Properties |
| | (000's) | (000's) | (000's) | (000's) |
| Operating Results - 3 months ended June 30: | | | | |
| Revenues: | | | | |
| Apartment rental income | \$ 17,508 | \$ - | \$ 1,830 | \$ 15,678 |
| Restaurant rental income | 957 | - | - | 957 |
| Management fee income | 11 | (92) | - | 103 |
| Interest and other income | 26 | (44) | 11 | 59 |
| | 18,502 | (136) | 1,841 | 16,798 |
| Expenses: | | | | |
| Apartment operations | 6,853 | (92) | 745 | 6,200 |
| Administration expenses | 1,375 | - | - | 1,375 |
| Interest and prepayment penalties | 5,728 | (44) | 637 | 5,135 |
| Depreciation | 4,157 | - | 197 | 3,960 |
| Amortization of deferred loan costs | 117 | - | 17 | 100 |
| Write-off of unamortized loan costs at debt refinance | 63 | - | - | 63 |
| Deficit distributions to minority partners of consolidated limited partnerships(2) | 800 | - | 800 | - |
| | 19,093 | (136) | 2,396 | 16,833 |
| (Loss) income before minority interest | (591) | \$ - | \$ (555) | \$ (35) |
| Loss (income) attributed to minority interests - | | | | |
| - Consolidated limited partnerships | 14 | | | |
| - Operating partnership | 171 | | | |
| Net (loss) income | (406) | | | |
| Cumulative preferred dividend | (250) | | | |
| (Loss) income attributed to common shareholders | \$ (656) | | | |
| (Loss) income before minority interest | \$ (591) | \$ - | \$ (555) | \$ (35) |
| Cumulative preferred dividend | (250) | - | - | (250) |
| Depreciation and amortization of real estate assets | 4,231 | - | 197 | 4,034 |
| Deficit distributions to minority | | | | |

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| | | | | |
|---|----------|-------|--------|----------|
| partners of consolidated limited partnerships(2) | 800 | - | 800 | - |
| | ----- | ----- | ----- | ----- |
| | 4,190 | - | 442 | 3,748 |
| Minority interest in FFO of consolidated limited partnerships | (200) | - | (200) | - |
| | ----- | ----- | ----- | ----- |
| Funds from operations(3) | \$ 3,990 | \$ - | \$ 242 | \$ 3,748 |
| | ===== | ===== | ===== | ===== |

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| | 2005 | | | |
|--|--------------|---------|----------------------|------------------|
| | Consolidated | Elim | Consolidated LPs (1) | Owned Properties |
| | (000's) | (000's) | (000's) | (000's) |
| Operating Results - 6 months ended June 30: | | | | |
| Revenues: | | | | |
| Apartment rental income | \$ 31,600 | \$ - | \$ 3,013 | \$ 28,586 |
| Restaurant rental income | 1,915 | - | - | 1,915 |
| Management fee income | 127 | (151) | - | 277 |
| Interest and other income | 251 | (56) | 5 | 302 |
| | ----- | ----- | ----- | ----- |
| | 33,892 | (207) | 3,018 | 31,081 |
| Expenses: | | | | |
| Apartment operations | 12,296 | (151) | 1,217 | 11,230 |
| Administration expenses | 2,934 | - | - | 2,934 |
| Interest and prepayment penalties | 10,818 | (56) | 1,548 | 9,326 |
| Depreciation | 7,678 | - | 543 | 7,135 |
| Amortization of deferred loan costs | 224 | - | 29 | 196 |
| Write-off of unamortized loan costs at debt refinance | 223 | - | 160 | 63 |
| Deficit distributions to minority partners of consolidated limited partnerships(2) | 7,621 | - | 7,621 | - |
| | ----- | ----- | ----- | ----- |
| | 41,794 | (207) | 11,119 | 30,882 |
| | ----- | ----- | ----- | ----- |
| (Loss) income before minority interest | (7,902) | \$ - | \$ (8,100) | \$ 199 |
| | ===== | ===== | ===== | ===== |
| Loss (income) attributed to minority interests - | | | | |
| - Consolidated limited partnerships | 76 | | | |
| - Operating partnership | 1,463 | | | |
| | ----- | | | |
| Net (loss) income | (6,363) | | | |
| Cumulative preferred dividend | (500) | | | |

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| | | | | |
|--|------------|------|------------|----------|
| (Loss) income attributed to common shareholders | ----- | | | |
| | \$ (6,863) | | | |
| | ===== | | | |
| (Loss) income before minority interest | \$ (7,902) | \$ - | \$ (8,100) | \$ 199 |
| Cumulative preferred dividend | (500) | - | - | (500) |
| Depreciation and amortization of real estate assets | 7,752 | - | 543 | 7,209 |
| Deficit distributions to minority partners of consolidated limited partnerships(2) | 7,621 | - | 7,621 | - |
| | ----- | | | |
| | 6,971 | - | 64 | 6,907 |
| Minority interest in FFO of consolidated limited partnerships | 338 | - | 338 | - |
| | ----- | | | |
| Funds from operations(3) | \$ 7,310 | \$ - | \$ 402 | \$ 6,907 |
| | ===== | | | |

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| | | | | |
|--|--------------|------------|----------------------|------------------|
| | ----- | | | |
| | 2005 | | | |
| | ----- | | | |
| | Consolidated | Elim | Consolidated LPs (1) | Owned Properties |
| | (000's) | (000's) | (000's) | (000's) |
| | ----- | | | |
| Balance Sheet at June 30, 2005, compared to December 31, 2004: | | | | |
| Real estate investments | \$484,927 | \$ - | \$40,004 | \$444,923 |
| Cash and cash equivalents | 2,533 | - | 696 | 1,837 |
| Prepaid expenses and other assets | 8,209 | (3,949) | 1,141 | 11,018 |
| Intangible assets, net | 1,251 | - | - | 1,251 |
| Deferred financing costs, net | 2,329 | - | 599 | 1,730 |
| | ----- | | | |
| | \$499,250 | \$ (3,949) | \$42,439 | \$460,760 |
| | ===== | | | |
| Deed of trust and other notes payable | \$410,480 | \$ (1,914) | \$47,625 | \$364,769 |
| Accounts payable and accrued expenses | 3,700 | (73) | 280 | 3,493 |
| Accrued interest | 1,721 | - | 190 | 1,531 |
| Consideration due for acquisitions | 1,000 | - | - | 1,000 |
| Deferred revenue and security deposits | 2,089 | - | 133 | 1,956 |
| | ----- | | | |
| | 418,989 | (1,987) | 48,228 | 372,748 |
| Minority interests - Consolidated limited partnerships | | | | |

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| | | | | |
|-------------------------|-----------|-----------|----------|-----------|
| | 274 | - | 274 | - |
| - Operating partnership | 19,637 | - | - | 19,637 |
| Shareholders' equity | 60,350 | (1,962) | (6,062) | 68,375 |
| | \$499,250 | \$(3,949) | \$42,439 | \$460,760 |
| | \$499,250 | \$(3,949) | \$42,439 | \$460,760 |

- (1) Effective January 26, 2005, we include the accounts of the Marina Shores Partnership and the Villages Partnership in our consolidated financial statements.
- (2) In accordance with generally accepted accounting principles ("GAAP"), deficit distributions to minority partners are charges recognized in our statement of operations when cash is distributed to a non-controlling partner in a consolidated limited partnership in excess of the positive balance in such partner's capital account (which is classified as minority interest in our consolidated balance sheet). We are required to record these charges for GAAP purposes even though there is no economic effect or cost to the company or the operating partnership.
- (3) See discussion of funds from operations under the caption "Funds from Operations" below in this Item 2.

Revenues

Total revenues in the second quarter of 2005 were \$18.5 million, compared to \$11.9 million in the second quarter of 2004. Total revenues in the first six months of 2005 were \$33.9 million, compared to \$23.1 million in the first six months of 2004. These increases are primarily attributable to increases in apartment rental income.

Apartment rental income totaled \$17.5 million in the second quarter of 2005, an increase of \$6.9 million, or 65.5%, compared to the second quarter of 2004. Apartment rental income in the first six months of 2005 totaled \$31.6 million, an increase of \$11.0 million, or 53.2%, compared to the first six months of 2004. These increases are attributable to:

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- o Apartment acquisitions in 2004 and 2005 - these ten communities contributed \$5.3 million in second quarter 2005 and \$7.9 million in the first six months of 2005, compared to \$0.4 million in the second quarter and first six months of 2004 (contributed by one community acquired in May 2004).
- o Apartment communities that we consolidate effective January 2005 - these two communities contributed \$1.8 million in second quarter 2005 and \$3.0 million in the first six months of 2005.

On a "same-units" basis (the 20 apartment communities that we owned as of January 1, 2004), apartment rental income increased by 2.4% in the second quarter and by 2.2% in the first six months of 2005 compared to 2004. These increases are consistent with increases in average revenue per occupied unit, while average economic occupancy for these units varied only slightly from comparable periods in 2004.

On a same-units basis, apartment NOI (apartment rental income less apartment operating expenses) for the second quarter of 2005 increased by 7.2% compared to the second quarter of 2004. For the first six months of 2005, same-units NOI increased by 4.8% compared to the first six months of 2004.

Summary amounts for our apartment communities' occupancy and revenue per occupied unit for the second quarter and first six months of 2005 follow:

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| | Number of apartment units | Three months ended June 30, 2005 | | Six mont June 30 |
|------------------------------|------------------------------------|-------------------------------------|--|----------------------------------|
| | | Average economic occupancy | Average monthly revenue per occupied unit | Average economic occupancy |
| Owned apartment communities: | | | | |
| Same-units communities: | | | | |
| Abbington Place | 360 | 95.8% | \$ 781 | 94.4% |
| Allerton Place | 228 | 94.5% | 797 | 94.6% |
| Barrington Place | 348 | 94.5% | 767 | 93.4% |
| Brookford Place | 108 | 95.4% | 677 | 96.5% |
| Chason Ridge | 252 | 91.9% | 797 | 92.1% |
| The Harrington | 288 | 90.1% | 787 | 92.5% |
| Harris Hill | 184 | 94.6% | 639 | 95.7% |
| Latitudes | 448 | 96.0% | 976 | 96.5% |
| Madison Hall | 128 | 97.3% | 590 | 95.8% |
| Marina Shores Waterfront | 290 | 94.5% | 847 | 94.3% |
| Oakbrook | 162 | 96.3% | 723 | 95.2% |
| Oak Hollow | 461 | 97.5% | 611 | 96.4% |
| Paces Commons | 336 | 94.9% | 649 | 95.5% |
| Paces Village | 198 | 98.0% | 674 | 96.7% |
| Pepperstone | 108 | 97.7% | 686 | 98.0% |
| Savannah Place | 172 | 94.5% | 724 | 95.0% |
| Summerlyn Place | 140 | 96.6% | 828 | 94.5% |
| The Place | 144 | 94.1% | 561 | 94.5% |
| Waterford Place | 240 | 95.6% | 888 | 93.5% |
| Woods Edge | 264 | 95.9% | 683 | 95.0% |

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| | Number of apartment units | Three months ended June 30, 2005 | | Six mont June 30 |
|-----------------------|------------------------------------|-------------------------------------|--|----------------------------------|
| | | Average economic occupancy | Average monthly revenue per occupied unit | Average economic occupancy |
| Acquired in 2004: | | | | |
| Carriage Club | 268 | 95.8% | 751 | 95.1% |
| Fairington | 250 | 95.4% | 724 | 96.0% |
| Savannah Shores | 198 | 96.4% | 804 | 94.3% |
| Bridges at Southpoint | 192 | 95.6% | 699 | 95.8% |
| Bridges at Wind River | 346 | 95.5% | 801 | 93.1% |

Acquired in 2005:

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| | | | | |
|--------------------------------------|-------|-------|-------|-------|
| Canterbury (3/31/05) | 630 | 97.7% | 607 | 97.7% |
| Laurel Springs (3/31/05) | 336 | 95.3% | 689 | 95.3% |
| Paces Watch (5/12/05) | 232 | 97.0% | 813 | 97.0% |
| Salem Ridge (3/31/05) | 120 | 97.7% | 531 | 97.7% |
| Waverly Place (4/21/05) | 240 | 93.6% | 670 | 93.6% |
| All apartments | | | | |
| - 2005 | 7,671 | 95.5% | 732 | 94.9% |
| - 2004 | 5,205 | 95.0% | 735 | 95.0% |
| Same units | | | | |
| - 2005 | | 95.2% | 750 | 94.9% |
| - 2004 | | 95.1% | 732 | 95.0% |
| Consolidated limited partnerships: | | | | |
| Marina Shores(1) | 392 | 97.2% | 1,160 | 95.6% |
| Villages of Chapel Hill(1) | 264 | 92.7% | 678 | 94.3% |
| Unconsolidated limited partnerships: | | | | |
| Villages - Phase 5(2) | 57 | 95.9% | 780 | 97.1% |

(1) We include the activities of these communities in our consolidated financial statements effective January 26, 2005.

(2) We acquired a 1% interest as general partner in this partnership effective January 26, 2005.

Restaurant rental income was \$957,000 in second quarter, and \$1.9 million through the first six months of both 2005 and 2004. We received the minimum rent specified in the lease agreement in the first two quarters of both 2005 and 2004. We currently hold 40 restaurant properties under this lease, and minimum rent is currently set at \$319,000 per month, or \$3.8 million per year.

Management fee income totaled \$11,000 in the second quarter of 2005, compared to \$208,000 in the second quarter of 2004. Management fee income totaled \$127,000 in the first six months of 2005, compared to \$405,000 in the first six months of 2004. These decreases are attributable to the elimination of management fees for Marina Shores and Villages of Chapel Hill with consolidation of these properties effective January 2005 and our acquisition of four managed

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properties effective March 31, 2005. Going forward, we expect that management fees will be insignificant.

Expenses

Total expenses were \$19.1 million in the second quarter of 2005, compared to \$11.6 million in the second quarter of 2004. Total expenses were \$41.8 million in the first six months of 2005, compared to \$22.5 million in the first six months of 2004. These increases are primarily attributable to growth in the size of our apartment operations, along with charges for deficit distributions to a minority partner.

We reflect the unaffiliated partners' interests in Marina Shores Associates One Limited Partnership ("Marina Shores Partnership") and The Villages of Chapel Hill Limited Partnership ("Villages Partnership") as minority interest in consolidated limited partnerships. Minority interest in consolidated limited partnerships represents the minority partners' share of the underlying net assets of these consolidated limited partnerships. When these consolidated

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limited partnerships make cash distributions to partners in excess of the carrying amount of the minority interest, we record a charge equal to the amount of such excess distributions, even though there is no economic effect or cost to the operating partnership. We report this charge in our consolidated statements of operations as deficit distributions to minority partners. We recorded charges for deficit distributions to the minority partner in the Marina Shores Partnership totaling \$6.8 million in the first quarter and \$0.8 million in the second quarter of 2005.

Apartment operations expense (the direct costs of on-site operations at our apartment communities) totaled \$6.9 million in the second quarter of 2005, an increase of \$2.5 million, or 56.2%, compared to the second quarter of 2004. Apartment operations expense in the first six months of 2005 totaled \$12.3 million, an increase of \$4.0 million, or 49.0%, compared to the first six months of 2004. These increases are primarily attributable to:

- o Apartment acquisitions in 2004 and 2005 - apartment operations expense for these ten communities was \$2.1 million in second quarter 2005 and \$3.3 million in the first six months of 2005, compared to \$0.1 million in the second quarter and first six months of 2004 (contributed by one community acquired in May 2004).
- o Apartment communities that we consolidate effective January 2005 - apartment operations expense for these two communities was \$0.7 million in second quarter 2005 and \$1.1 million in the first six months of 2005.

On a same-units basis, apartment operations expense declined by 4.2% in the second quarter and 1.8% in the first six months of 2005 compared to 2004, due primarily to reductions in compensation and property insurance costs.

Operating expenses for restaurant properties are insignificant because the triple-net lease arrangement requires the lessee to pay virtually all of the expenses associated with the restaurant properties.

Apartment administration costs (the costs associated with oversight, accounting and support of our apartment management activities) totaled \$0.7 million in the second quarter of 2005, a 20.2% increase compared to the second quarter of 2004. Apartment administration costs totaled \$1.4 million in the first six months of 2005, a 35.7% increase compared to the first six months of 2004. These increases are primarily attributable to additional corporate support staff.

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Corporate administration expense totaled \$0.6 million in the second quarter of 2005, an increase of 13.5% compared to the second quarter of 2004. Corporate administration costs totaled \$1.5 million in the first six months of 2005, an increase of 24.0% compared to the first six months of 2004. These increases are primarily attributable to a \$0.2 million increase in professional fees associated with requirements of Section 404 of the Sarbanes-Oxley Act of 2002 and late audit fee billings.

Depreciation expense totaled \$4.2 million in the second quarter of 2005, an increase of \$1.5 million, or 54.5%, compared to the second quarter of 2004. Depreciation expense totaled \$7.7 million in the first six months of 2005, an increase of \$2.4 million, or 46.8%, compared to the first six months of 2004. These increases are primarily attributable to acquisitions of apartment communities (\$2.0 million in the first six months of 2005), along with depreciation expense for the two apartment communities that we consolidate effective January 2005, which totaled \$0.5 million in the first six months of 2005.

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Interest expense totaled \$5.7 million in the second quarter of 2005, an increase of \$2.4 million, or 72.0%, compared to the second quarter of 2004. Interest expense (including \$0.5 million in prepayment penalties paid by Marina Shores) totaled \$10.8 million in the first six months of 2005, an increase of \$4.2 million, or 64.7%, compared to the first six months of 2004. This increase is primarily attributable to new debt issued in conjunction with acquisitions of apartment properties during 2004 and 2005, along with the impact of consolidating Marina Shores and Villages of Chapel Hill effective January 2005. Overall, weighted average interest rates were 5.8% for the second quarter and first six months of 2005, compared to 5.7% for the second quarter and first six months of 2004, reflecting the impact of steady increases in variable interest rates over the last twelve months.

Net Income

Consolidated earnings before non-cash charges (for depreciation, amortization and write-off of unamortized loan costs at refinance) and before the \$0.8 charge for deficit distributions to a minority partner (which has no economic effect or cost to the operating partnership) totaled \$4.5 million, an increase of \$1.6 million, or 53.3%, compared to the second quarter of 2004. Consolidated earnings before non-cash charges and before the \$7.6 million charge for deficit distributions to a minority partner in the first six months of 2005 totaled \$7.8 million, a \$1.8 million, or 30.7%, increase compared to the first six months of 2004. These increases reflect the positive impact of new apartment communities and improvements in apartment revenues, offset by a \$0.5 million charge for prepayment penalties paid at loan refinance by a consolidated limited partnership during the first quarter of 2005.

On a consolidated basis, before minority interests in the consolidated limited partnerships and the minority interest in the operating partnership, the net loss for the second quarter of 2005 totaled \$0.6 million, compared to \$0.2 million in income before minority interests in the second quarter of 2004. The net loss before minority interests in the first six months of 2005 totaled \$7.9 million, compared to \$0.6 million in income before minority interest in the first six months of 2004. The 2005 losses again reflect the impact of charges for deficit distributions to a minority partner (\$0.8 million in the second quarter and \$7.6 million in the first six months), a first quarter 2005 charge of \$0.5 million for penalties paid at loan refinance by a consolidated limited partnership, along with additional \$0.2 million charges to write off unamortized loan costs at refinance.

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We allocate proportional income and losses of the consolidated limited partnerships to minority partners to the extent of the carrying amount of the minority interest. We record a charge when losses attributable to the consolidated limited partners of a consolidated limited partnership exceed the carrying amount of the minority interest, even though there is no economic effect or cost to the operating partnership. During the first quarter of 2005 we recorded charges for consolidated limited partnership losses, resulting primarily from depreciation and costs related to refinance of the Partnership's first deed of trust loan, of approximately \$621,000 that were not allocated to the minority partner in Marina Shores Partnership because the losses exceeded the carrying amount of the minority interest. During the second quarter of 2005, we reduced these charges by \$203,000 for income that would otherwise have been allocated to the limited partner.

Minority interests in the Villages Partnership and the operating partnership absorbed \$0.2 million in the second quarter of 2005, and \$1.5 million in the first six months, of the consolidated losses. After allocating

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those losses to minority interests, the net loss was \$0.4 million in the second quarter of 2005 and \$6.4 million in the first six months of 2005.

Because the preferred shareholder has priority over common shareholders for receipt of dividends, we deduct the amount of net income that will be paid to the preferred shareholder in calculating net income available to common shareholders. After deducting \$250,000 for the cumulative preferred dividend in each of the first two quarters of both 2005 and 2004, the net loss attributed to common shareholders was \$0.7 million for the second quarter and \$6.9 million for the first six months of 2005, compared to essentially break-even amounts for the second quarter and first six months of 2004.

Funds from Operations

Funds from operations is frequently referred to as "FFO." FFO is defined by the National Association of Real Estate Investment Trusts ("NAREIT") as "net income (computed in accordance with generally accepted accounting principles), excluding gains (losses) from sales of property, plus depreciation and amortization, and after adjustments for unconsolidated partnerships and joint ventures." Our calculation of FFO is consistent with FFO as defined by NAREIT. Because we hold all of our assets in and conduct all of our operations through the operating partnership, we measure FFO at the operating partnership level (i.e., after deducting the minority interests in FFO of the consolidated limited partnerships, but before deducting the minority interest in the operating partnership).

Historical cost accounting for real estate assets implicitly assumes that the value of real estate assets diminishes predictably over time. In fact, real estate values have historically risen or fallen with market conditions. FFO is intended to be a standard supplemental measure of operating performance that excludes historical cost depreciation from - or "adds it back" to - GAAP net income. We consider FFO to be useful in evaluating potential property acquisitions and measuring operating performance.

Funds available for distribution is frequently referred to as "FAD." We define FAD as FFO plus non-cash expense for amortization and write-off of unamortized loan costs, plus (less) gains (losses) from sales of property, less recurring capital expenditures. We believe that, together with net income and cash flows from operating activities, FAD provides investors with an additional measure to evaluate the ability of the operating partnership to incur and service debt, to fund acquisitions and other capital expenditures, and to fund distributions to shareholders and minority unitholders.

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Funds from operations and funds available for distribution do not represent net income or cash flows from operations as defined by generally accepted accounting principles. Nor do FFO or FAD measure whether cash flow is sufficient to fund all of our cash needs, including principal amortization, capital improvements and distributions to shareholders and unitholders. You should not consider FFO or FAD to be alternatives to net income as reliable measures of the company's operating performance; nor should you consider FFO or FAD to be alternatives to cash flows from operating, investing or financing activities (as defined by generally accepted accounting principles) as measures of liquidity. Further, FFO and FAD as disclosed by other REITs might not be comparable to our calculation of FFO or FAD.

Funds from operations totaled \$4.0 million in the second quarter of 2005, an increase of 50.7% compared to the second quarter of 2004. Funds from operations in the first six months of 2005 totaled \$7.3 million, an increase of 36.7% compared to the first six months of 2004. These comparisons reflect the

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positive impact of apartment additions and the improvement in apartment operating results.

We calculated FFO of the operating partnership as follows:

| | Three months ended June 30 | | Six months ended June 30 | |
|--|-------------------------------|----------|-----------------------------|------------|
| | 2005 | 2004 | 2005 | 2004 |
| | (000's) | (000's) | (000's) | (000's) |
| (Loss) income before minority interest | \$ (591) | \$ 208 | \$ (7,902) | \$ (7,902) |
| Less cumulative preferred dividend | (250) | (250) | (500) | (500) |
| Add amortization of in-place lease intangibles | 74 | - | 74 | - |
| Add depreciation | 4,157 | 2,690 | 7,678 | 7,678 |
| Add deficit distributions to minority partners of consolidated limited partnerships(1) | 800 | - | 7,621 | - |
| Less minority interest in FFO of consolidated limited partnerships | (200) | - | 338 | - |
| Funds from operations | \$ 3,990 | \$ 2,648 | \$ 7,310 | \$ 7,310 |

- (1) In accordance with GAAP, deficit distributions to minority partners are charges recognized in our statement of operations when cash is distributed to a non-controlling partner in a consolidated limited partnership in excess of the positive balance in such partner's capital account (which is classified as minority interest in our consolidated balance sheet). We are required to record these charges for GAAP purposes even though there is no economic effect or cost to the operating partnership.

Deficit distributions to minority partners may occur when the fair value of the underlying real estate exceeds its depreciated net book value because the underlying real estate has appreciated or maintained its value. As a result, deficit distributions to minority partners represent, in substance, either our recognition of depreciation previously allocated to the non-controlling partner or a cost related to the non-controlling partner's share of real estate appreciation. Based on NAREIT guidance that requires that real estate depreciation and gains be excluded from FFO, we add back deficit distributions and subtract related recoveries in our reconciliation of net income to FFO.

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A reconciliation of net cash provided by operating activities (as defined by generally accepted accounting principles and reflected in our consolidated statements of cash flows) to FAD follows:

| | Three months ended June 30 | | Six months ended June 30 | |
|--|-------------------------------|------|-----------------------------|------|
| | 2005 | 2004 | 2005 | 2004 |
| | | | | |

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| | (000's) | (000's) | (000's) |
|---|----------|----------|----------|
| Net cash provided by operating activities | \$ 4,371 | \$ 2,325 | \$ 7,048 |
| Less recurring capital expenditures | (844) | (626) | (1,302) |
| Less cumulative preferred dividend | (250) | (250) | (500) |
| Add (less) change in net operating assets and liabilities | 204 | 614 | 794 |
| Add amortization of deferred interest defeasance | 46 | 26 | 77 |
| Add (less) minority interest in consolidated limited partnerships' share of reconciling items | (162) | - | 221 |
| Funds available for distribution | \$ 3,364 | \$ 2,089 | \$ 6,338 |

Other information about our historical cash flows follows (all amounts in thousands):

| | Three months ended June 30 | | Six months ended June 30 |
|--|-------------------------------|----------|-----------------------------|
| | 2005 | 2004 | 2005 |
| | (000's) | (000's) | (000's) |
| Net cash provided by (used in): | | | |
| Operating activities | \$ 4,371 | \$ 2,325 | \$ 7,048 |
| Investing activities | (37,717) | (20,510) | (39,564) |
| Financing activities | 33,296 | 21,988 | 34,532 |
| Dividends and distributions paid to: | | | |
| Preferred shareholders | \$ 250 | \$ 250 | \$ 500 |
| Common shareholders | 2,308 | 1,775 | 4,580 |
| Minority partners in consolidated limited partnerships | 800 | - | 7,621 |
| Minority unitholders in operating partnership | 450 | 460 | 916 |
| Scheduled debt principal payments | 577 | 297 | 1,020 |
| Non-recurring capital expenditures | 1,962 | 359 | 2,795 |

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| | Three months ended June 30 | | Six months ended June 30 |
|-------------------------------------|-------------------------------|---------|-----------------------------|
| | 2005 | 2004 | 2005 |
| | (000's) | (000's) | (000's) |
| Weighted average shares outstanding | | | |
| Preferred shares | 909 | 909 | 909 |
| Common shares | 9,239 | 7,119 | 9,111 |

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Weighted average operating partnership
minority units outstanding

2,408 1,850 2,141

Capital Resources and Liquidity

Capital Resources

We completed a number of significant investing and financing transactions during the second quarter and first six months of 2005.

Acquisition of Boddie Investment Company

In January 2005, we acquired Boddie Investment Company ("BIC") through a merger. We issued 508,578 shares of our common stock, and cancelled 72,399 shares of common stock that BIC held immediately before the merger. The value of this transaction was \$8.2 million. Direct costs (out-of-pocket cash costs) related to this acquisition were approximately \$150,000. As a result of this acquisition, we assumed the role of general partner and acquired certain economic interests in three limited partnerships. Prior to this acquisition, we managed the apartment communities owned by these partnerships on a contract basis; we will continue to manage these partnerships.

A summary of assets acquired in the BIC acquisition, along with our preliminary allocation of costs assigned to those assets, follows (amounts in thousands):

Investments in limited partnerships:

| | |
|---|---------|
| Marina Shores Associates One, Limited Partnership | \$5,940 |
| The Villages of Chapel Hill Limited Partnership | 2 |
| The Villages of Chapel Hill - Phase 5 Limited Partnership | 7 |
| BNP common stock held by BIC (which we immediately retired) | 1,166 |
| Receivables from the Villages Partnership for general partners' advances and accrued interest thereon | 1,220 |
| | ----- |
| | \$8,335 |
| | ===== |

Although the amounts related to this acquisition seem relatively insignificant at first glance, the accounting for the investments in limited partnerships is complex, and the impact on presentation of our consolidated financial statements is rather significant. We have included a detailed discussion of our accounting treatment for each of the investments in limited partnerships in Note 2 of our financial statements included in this Current Report on Form 10-Q. A summary of that discussion for each limited partnership follows:

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BIC Acquisition - Marina Shores Partnership

We acquired a 50% general partner interest in the Marina Shores Partnership. Under the terms of the partnership agreement for the Marina Shores Partnership, the general partner controls the activities of the partnership. We have therefore included the accounts of this partnership in our consolidated financial statements effective January 26, 2005. In our preliminary accounting for the BIC acquisition, the initial inclusion of the Marina Shores Partnership in our consolidated financial statements resulted in (amounts in thousands):

| | |
|---|----------|
| Increase in real estate investments - 392 apartment units | \$26,254 |
|---|----------|

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| | |
|---------------------------------------|----------|
| Increase in cash and cash equivalents | 252 |
| Increase in other assets | 1,251 |
| | ----- |
| | 27,757 |
| | |
| Increase in long-term debt | 20,745 |
| Increase in other liabilities | 1,072 |
| | ----- |
| | 21,817 |
| | ----- |
| Increase in net assets | \$ 5,940 |
| | ===== |

Very shortly after our acquisition of BIC, the Marina Shores Partnership completed a refinancing of its long-term debt. The Marina Shores Partnership issued a \$33.9 million fixed-rate note payable. This 10-year loan provides for interest at an effective rate of 5.1%. The Marina Shores Partnership first applied proceeds of this loan to retire the existing \$20.7 million deed of trust loan balance along with \$1.2 million interest and prepayment penalties, then distributed \$6.8 million to its limited partner and \$3.7 million to the operating partnership. During the second quarter of 2005, the Marina Shores Partnership made additional distributions of \$0.8 million to its limited partner and \$0.3 million to the operating partnership.

Prior to consolidation in our financial statements, the fair value of the real estate held by the Marina Shores Partnership significantly exceeded its depreciated net book value because the underlying real estate had appreciated significantly since the Marina Shores Partnership's original formation in the late 1980s. In our initial consolidation of this partnership, we reset the noncontrolling limited partner's capital account to \$-0-. Distributions to the limited partner subsequent to inclusion of the Marina Shores Partnership in our consolidated financial statements are, and will generally be, reflected as charges against income in our consolidated financial statements as "deficit distributions to minority partners."

In accordance with GAAP, deficit distributions to minority partners are charges recognized in our income statement when cash is distributed to a non-controlling partner in a consolidated limited partnership in excess of the positive balance in such partner's capital account (which is classified as minority interest in our consolidated balance sheet). Deficit distributions to minority partners represent, in substance, either (a) our recognition of depreciation previously allocated to the non-controlling partner or (b) a cost related to the non-controlling partner's share of real estate appreciation. We record these charges for GAAP purposes even though there is no economic effect or cost to the company or the operating partnership.

BIC Acquisition - The Villages Partnership

We acquired a 1% general partner interest in the Villages Partnership. We determined that, in accordance with GAAP, the Villages Partnership is a "variable interest entity" ("VIE")

because it does not have sufficient equity to carry out its principal activities without additional subordinated financial support, and that we are the "primary beneficiary" of the Partnership. We have therefore included the accounts of this partnership in our consolidated financial statements effective January 26, 2005. In our preliminary accounting for the BIC acquisition, the initial inclusion of the Villages Partnership in our consolidated financial statements resulted in

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(amounts in thousands):

| | |
|---|----------|
| Increase in real estate investments - 264 apartment units | \$14,188 |
| Increase in cash and cash equivalents | 87 |
| Increase in other assets | 318 |
| | ----- |
| | 14,594 |
| | |
| Increase in long-term debt - first deed of trust | 12,094 |
| Increase in subordinated long-term debt to BNP* | 1,888 |
| Increase in other liabilities | 260 |
| Minority interest in consolidated limited partnerships | 350 |
| | ----- |
| | 14,592 |
| | ----- |
| | |
| Increase in net assets | \$ 2 |
| | ===== |

*The subordinated long-term debt to BNP is eliminated in consolidation against related receivable balances.

BIC Acquisition - The Villages of Chapel Hill - Phase 5 Limited Partnership

We acquired a 1% general partner interest in The Villages of Chapel Hill - Phase 5 Limited Partnership ("Villages - Phase 5 Partnership"). Under the terms of the partnership agreement for the Villages - Phase 5 Partnership and consistent with GAAP in place in January 2005, the limited partners have certain voting rights that preclude control by the general partner. We have therefore accounted for our investment in this partnership by applying the equity method. Our initial investment in the Villages - Phase 5 Partnership was \$7,000, and we include this amount in "other assets" on our consolidated balance sheet.

In late June 2005, the FASB ratified its Emerging Issues Task Force consensus in Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners have Certain Rights" ("Issue 04-5"). This new guidance states that the general partner in a limited partnership is presumed to control that limited partnership, with very limited exceptions. We have not yet made a final determination as to how the provisions of this new guidance will impact our accounting treatment for our interest in the Villages - Phase 5 Partnership. We may be required to consolidate the accounts of the Villages - Phase 5 Partnership beginning no later than January 1, 2006; however, we do not expect that such a change in accounting treatment would have a material effect on our financial statements.

Acquisition of Shugart Properties

On March 31, 2005, we completed the acquisition of a portfolio of four apartment properties from entities that we call the "Shugart Parties." The aggregate purchase price for the properties totaled \$52.1 million, including approximately \$0.3 million in net operating assets, paid through assumption or refinancing of \$42.8 million of debt on the properties and \$9.3 million paid in operating partnership units with an imputed value of \$13.50 per unit. Under the

terms of the exchange agreements, we issued 689,000 operating partnership units at closing, and will issue an additional 74,000 deferred units in March 2006. The preliminary allocation of the purchase price includes the following significant components:

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| Property | Apt. Units | Contract Price | Debt Assumed | Val Oper Partner |
|------------------------------|---------------|----------------|--------------|------------------------|
| | | (000's) | (000's) | (00 |
| Canterbury Apartments | 630 | \$ 25,750 | \$ 22,992 | \$ |
| Laurel Springs Apartments | 240 | 14,610 | 11,320 | |
| Laurel Springs II Apartments | 96 | 7,090 | 5,850 | |
| Salem Ridge Apartments | 120 | 4,360 | 2,610 | |

We will operate Laurel Springs and Laurel Springs II Apartments as one community. The assets and liabilities of these apartment communities are included in our consolidated financial statements as of March 31, 2005. However, no operating results for these communities are reflected in our consolidated statement of operations for the first quarter of 2005.

Immediately upon completion of this acquisition, we retired a \$1.5 million variable rate note related to Canterbury Apartments. The remaining assumed debt includes three fixed-rate notes totaling \$35.4 million at interest rates ranging from 5.0% to 6.8% and a \$5.9 million variable-rate note with interest at 30-day LIBOR plus 1.9%. We have included a more detailed description of these notes payable in Note 4 of our financial statements in this Current Report on Form 10-Q.

Other acquisitions

During the second quarter of 2005, we completed two additional apartment property acquisitions in separate cash transactions. Both properties are located in the Charleston, South Carolina, area.

| Property | Apt. Units | Contract Price |
|--------------------------|---------------|----------------|
| | | (000's) |
| Waverly Place Apartments | 240 | \$13,100 |
| Paces Watch Apartments | 232 | \$20,450 |

In conjunction with these acquisitions, we issued two fixed-rate notes payable totaling \$25.0 million. Both notes provide for interest at 5.31% (5.38% effective rate), interest-only payments through mid-2008, and then amortizing payments through mid-2015. A more detailed description of these notes payable is included in Note 4 of our financial statements in this Current Report on Form 10-Q.

In addition, during the second quarter of 2005, we acquired approximately 40 acres of undeveloped land adjacent to our Canterbury Apartments property for a contract price of \$2.7 million, paid by \$0.6 million in cash and the assumption of \$2.1 million in debt, which bears interest at the lender's prime rate and matures in September 2005.

Debt refinancing transactions

During the second quarter of 2005, in conjunction with refinancing of existing debt, we issued two fixed-rate notes payable totaling \$22.6 million.

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The new notes provide for interest at 5.21% (5.28% effective rate), interest-only payments through mid-2008, and then amortizing payments through mid-2015. We applied proceeds of these notes to retire an \$11.5 million variable-rate note payable, to retire a \$5.5 million 8.55% fixed-rate note payable, and to reduce the outstanding balance on our line of credit. A more detailed description of these transactions is included in Note 4 of our financial statements in this Current Report on Form 10-Q.

Other equity transactions

During the first and second quarters of 2005, we also:

- o Issued 25,000 shares of our common stock through our Dividend Reinvestment and Stock Purchase Plan for proceeds of \$0.4 million;
- o Issued 57,500 shares of our common stock upon exercise of options by two employees for proceeds of \$0.7 million; and
- o Issued 73,000 shares of our common stock to redeem the same number of operating partnership units from a minority unitholder.

At June 30, 2005, we had 9.2 million common shares and 0.9 million preferred shares outstanding. In addition, there were 2.4 million operating partnership minority common units outstanding.

Subsequent to the end of the second quarter of 2005, as of August 1, 2005, the Board of Directors granted restricted stock awards for a total of 200,000 shares of common stock to four members of the company's senior management. The shares vest annually at the rate of 10% per year, and carry all rights of ownership, including the receipt of dividends.

Cash Flows and Liquidity

Net cash flows from operating activities were \$4.4 million in the second quarter of 2005, compared to \$2.3 million in the second quarter of 2004. Net cash flows from operating activities were \$7.0 million in the first six months of 2005, compared to \$5.7 million in the first six months of 2004. The amounts for 2005 include a \$0.5 million prepayment penalty paid by the Marina Shores Partnership in conjunction with refinance of its long-term debt in first quarter. The increases in comparative amounts reflect the growth in size of our apartment operations.

Investing and financing activities, other than those described under "Capital Resources" above, focused on capital expenditures at apartment communities, along with payment of dividends and distributions.

We have announced that the company will pay a regular quarterly dividend of \$0.25 per share (approximately \$2.4 million) on August 15, 2005, to shareholders of record of our common stock as of August 1, 2005, as well as \$250,000 of dividends to the preferred shareholder.

We generally expect to meet our short-term liquidity requirements through net cash provided by operations and utilization of credit facilities. We believe that net cash provided by operations is, and will continue to be, adequate to meet the REIT operating requirements in both the short term and the long term. We anticipate funding our future acquisition activities primarily

by using short-term credit facilities as an interim measure, to be replaced by funds from equity offerings, long-term debt or joint venture investments. We expect to meet our long-term liquidity requirements, such as scheduled debt

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maturities and repayment of short-term financing of future property acquisitions, through long-term secured and unsecured borrowings and the issuance of debt securities or additional equity securities. We believe we have sufficient resources to meet our short-term liquidity requirements.

Critical Accounting Policies

We identify and discuss our significant accounting policies in the notes to our financial statements included in our Annual Report on Form 10-K. Our policies and practice regarding our accounting for our general partner interests in limited partnerships and for capital expenditures and depreciation, which may be of particular interest to readers of this Quarterly Report, are further discussed below.

Accounting for VIEs

In January 2003, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation 46, "Consolidation of Variable Interest Entities," ("FIN 46"). In December 2003, the FASB modified FIN 46 to make certain technical corrections and address certain implementation issues that had arisen. FIN 46 provided a new framework for identifying VIEs and determining when a company should include the assets, liabilities, noncontrolling interests and results of activities of a VIE in its consolidated financial statements.

In general, a VIE is an entity or other legal structure used to conduct activities or hold assets that either (1) has an insufficient amount of equity to carry out its principal activities without additional subordinated financial support, (2) has equity owners that, as a group, are unable to make significant decisions about its activities, or (3) has equity owners that, as a group, do not have the obligation to absorb losses or the right to receive returns generated by its operations.

FIN 46, as modified, requires a VIE to be consolidated if a party with an ownership, contractual or other financial interest in the VIE (a "variable interest holder") is obligated to absorb a majority of the risk of loss from the VIE's activities, is entitled to receive a majority of the VIE's residual returns (if no party absorbs a majority of the VIE's losses), or both. A variable interest holder that consolidates the VIE is called the "primary beneficiary." Upon consolidation, the primary beneficiary generally must initially record all of the VIE's assets, liabilities and noncontrolling interests at fair value and subsequently account for the VIE as if it were consolidated based on majority voting interest. FIN 46 also requires disclosures about VIEs that the variable interest holder is not required to consolidate but in which it has a significant variable interest.

We determined that the Villages Partnership is a VIE, because the limited partnership does not have sufficient equity to carry out its principal activities without additional subordinated financial support from the general partner. We also determined that we are the primary beneficiary of the Villages Partnership. We have therefore included the accounts of this partnership in our consolidated financial statements effective January 26, 2005.

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Accounting for general partner interests in limited partnerships

As managing general partner in three real estate limited partnerships, we have the ability to exercise significant influence over operating and financial policies. This influence is evident in the terms of the respective partnership agreements. However, following guidance in SOP 78-9, we do not "control" the respective limited partnerships if the limited partners have

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significant rights, such as the right to replace the general partner and the right to approve the sale or refinancing of the assets of the respective partnership in accordance with the partnership agreement. In acting as the general partner in these limited partnerships, we are committed to providing additional levels of funding to meet partnership operating deficits as may be needed.

If we, as general partner, control a partnership that is not considered a VIE, generally accepted accounting principles require that the partnership be consolidated in our financial statements. Upon consolidation, we initially record our interest in the partnership's assets and liabilities at the lower of our cost or fair value, and subsequently account for the partnership based on our percentage interest; the non-controlling interests are reflected in our financial statements at their historical costs.

We determined that the Marina Shores Partnership is not a VIE. However, under the terms of the partnership agreement for the Marina Shores Partnership, the general partner controls the activities of partnership; we have therefore included the accounts of this partnership in our consolidated financial statements effective January 26, 2005.

We determined that the Villages - Phase 5 Partnership is not a VIE. Under the terms of the partnership agreement for the Villages - Phase 5 Partnership, the limited partners have certain voting rights that preclude control by the general partner under guidance in SOP 78-9. We have accounted for our investment in this partnership in January 2005 by applying the equity method. (See Note 2 to our financial statements included in this Current Report on Form 10-Q. Under recently issued guidance in EITF Issue 04-5, we may be required to consolidate these accounts in the near future; however, we do not expect that such a change in accounting treatment will have a material effect on our financial statements.)

Purchase price allocation for apartment community acquisitions

In connection with the acquisition of an apartment community, we perform a valuation and allocation to each asset and liability in such transaction, based on their estimated fair values at the date of acquisition. The valuation of assets acquired includes both tangible and intangible assets. Significant tangible asset values include real estate investments which are subsequently depreciated over their estimated useful lives. We include intangible asset values, consisting of at-market, in-place leases, in intangible assets and amortize these amounts over the remaining lease terms. In general, the average remaining life of in-place leases at acquisition date ranged from five to nine months, and intangible assets represented approximately 0.1% to 0.3% of contract prices.

Capital expenditures and depreciation

In general, for the 15 apartment properties acquired before 2002, we compute depreciation using the straight-line method over composite estimated useful lives of the related assets, generally 40 years for buildings, 20 years for land improvements, 10 years for fixtures and equipment, and five years for floor coverings.

For apartment properties acquired in 2002 and later, we have or will perform analyses of components of the real estate assets acquired. For these properties, we assign estimated useful lives as follows: base building structure, 43-60 years; land improvements, 7-20 years; short-lived building components, 5-20 years; and fixtures, equipment and floor coverings, 5-10 years.

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We generally complete and capitalize acquisition improvements (expenditures that have been identified at the time the property is acquired, and which are intended to position the property consistent with our physical standards) within one to two years of acquisition. We capitalize non-recurring expenditures for additions and betterments to buildings and land improvements. In addition, we generally capitalize recurring capital expenditures for exterior painting, roofing, and other major maintenance projects that substantially extend the useful life of existing assets. For financial reporting purposes, we depreciate these additions and replacements on a straight-line basis over estimated useful lives of 5-20 years. We retire replaced assets with a charge to depreciation for any remaining carrying value. We capitalize all floor covering, appliance and HVAC replacements, and depreciate them using a straight-line, group method over estimated useful lives of 5-10 years.

Capital expenditures at our owned apartment communities during the first six months of 2005 totaled \$4.4 million, including \$0.9 million for acquisition improvements, \$2.3 million for additions and betterments, and \$1.2 million for recurring capital expenditures.

We expense ordinary repairs and maintenance costs at apartment communities. Repairs and maintenance at our owned apartment communities during the first six months of 2005 totaled \$4.1 million, including \$1.5 million in compensation of service staff and \$2.6 million in payments for material and contracted services.

A summary of capital expenditures at our owned apartment communities through June 30, 2005, in aggregate and per apartment unit, follows:

| | Total | Per |
|---|----------|-------|
| | ----- | ----- |
| | (000's) | |
| Recurring capital expenditures: | | |
| Floor coverings | \$ 544 | |
| Appliances/HVAC | 234 | |
| Computer/support equipment | 8 | |
| Other | 422 | |
| | ----- | ----- |
| | \$ 1,208 | |
| | ===== | ===== |
| Non-recurring capital expenditures: | | |
| Acquisition improvements at apartment properties | \$ 843 | |
| Casualty replacements | 670 | |
| Additions and betterments at apartment properties | 1,611 | |
| Computer/support equipment | 45 | |
| | ----- | ----- |
| | \$ 3,169 | |
| | ===== | ===== |

Costs of repairs, maintenance, and capital replacements and improvements at restaurant properties are borne by the lessee.

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We completed a number of significant acquisition and financing transactions during the first six months of 2005.

As of June 30, 2005, long-term debt, on a consolidated basis, totaled \$410.5 million, including \$338.3 million of notes payable at fixed rates ranging from 5.0% to 7.1%, and \$72.2 million at variable rates indexed primarily on 30-day LIBOR rates. The weighted average interest rate on debt outstanding was 5.8% at June 30, 2005, compared to 5.9% at December 31, 2004. A 1% fluctuation in variable interest rates would increase or decrease our annual interest expense by approximately \$0.7 million.

The table below provides information about our long-term debt instruments and presents expected principal maturities and related weighted average interest rates on instruments in place as of June 30, 2005 (all amounts in thousands).

| | Expected maturity dates | | | | | |
|-----------------------|-------------------------|----------|----------|----------|----------|-----------|
| | 2005 | 2006 | 2007 | 2008 | 2009 | Later |
| Fixed rate notes | \$ 1,323 | \$ 2,884 | \$50,890 | \$42,793 | \$32,137 | \$208,254 |
| Average interest rate | 5.3% | 5.3% | 6.9% | 6.5% | 5.2% | 5.8% |
| Variable rate notes | \$ 200 | \$ 6,064 | \$28,231 | \$15,979 | \$21,725 | - |
| Average interest rate | 5.0% | 5.1% | 5.0% | 5.0% | 5.0% | - |

Item 4. Controls and Procedures

We maintain disclosure controls and procedures designed to ensure that information disclosed in our annual and periodic reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. In addition, we designed these disclosure controls and procedures to ensure that this information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, to allow timely decisions regarding required disclosures.

Based on our most recent evaluation, which was completed as of the end of the second quarter of 2005, our chief executive officer and chief financial officer believe that our disclosure controls and procedures are effective. There have been no significant changes in our internal controls or in other factors that could significantly affect the internal controls subsequent to the completion of this evaluation.

Part II - Other Information

Item 4. Submission of Matters to a Vote of Security Holders

We held our Annual Meeting of Shareholders on May 19, 2005. Of the 9,232,501 shares of common stock issued, outstanding, and entitled to vote at this meeting, 7,802,200, or 84.51%, were present in person or by proxy. The following proposals were approved:

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| | For | Against | Withheld/ Abstained |
|---|-----------|-----------|------------------------|
| Election of directors - | | | |
| -Election of directors to serve until the 2008 annual meeting: | | | |
| D. Scott Wilkerson | 6,287,674 | -0- | 1,514,526 |
| Paul G. Chrysson | 6,279,573 | -0- | 1,522,627 |
| -Election of a Series B director to serve until the 2006 annual meeting: | | | |
| Peter J. Weidhorn (elected by the holders of Series B Cumulative Preferred Stock) | 909,090 | -0- | -0- |
| Amendment to the Amended and Restated 1994 Stock Option and Incentive Plan | 3,733,022 | 1,990,173 | 29,096 |

Other directors, whose terms of office as directors continue after the meeting, are as follows:

Serving until the 2006 annual meeting:

 W. Michael Gilley Serving until the 2007 annual meeting:

 Philip S. Payne

 Stephen R. Blank

Item 5. Other Information

Re-appointment of officers

The Board of Directors re-appointed the following executive officers effective May 19, 2005:

| | |
|--------------------|--|
| Philip S. Payne | Chairman, Chief Financial Officer, and Assistant Secretary |
| D. Scott Wilkerson | President and Chief Executive Officer |
| Pamela B. Bruno | Vice President, Treasurer, Chief Accounting Officer, and Assistant Secretary |
| Eric S. Rohm | Vice President, Secretary, and General Counsel |

Effective as of August 1, 2005, Philip S. Payne resigned as chief financial officer of the company. Mr. Payne remains as chairman of the board of directors, which is an executive officer position with the company, and will continue to lead the development of corporate strategy and capital markets activities at the Company. Also effective as of August 1, 2005, the board of directors appointed Pamela B. Bruno as the company's chief financial officer.

Item 6. Exhibits

The Registrant agrees to furnish a copy of all agreements related to long-term debt upon request of the Commission.

Exhibit No.

10.1* Amended and Restated 1994 Stock Option and Incentive Plan, as amended May 19, 2005 (filed as Exhibit 10.1 to BNP Residential

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- Properties, Inc. Current Report on Form 8-K dated May 19, 2005,
and incorporated herein by reference)
- 31.1 Rule 13a-14(a)/15d-14(a) Certification by Chief Executive Officer
 - 31.2 Rule 13a-14(a)/15d-14(a) Certification by Chief Financial Officer
 - 32.1 Section 1350 Certification by Chief Executive Officer
 - 32.2 Section 1350 Certification by Chief Financial Officer

* Incorporated herein by reference

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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.

BNP RESIDENTIAL PROPERTIES, INC.
(Registrant)

August 5, 2005

/s/ Philip S. Payne

Philip S. Payne
Chairman

August 5, 2005

/s/ Pamela B. Bruno

Pamela B. Bruno
Vice President, Treasurer and
Chief Financial Officer

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INDEX TO EXHIBITS

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