SAUL CENTERS INC
Form 10-Q
November 09, 2009
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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 September 30, 2009

Commission File Number 1-12254

SAUL CENTERS, INC.

(Exact name of registrant as specified in its charter)

Maryland	**52-1833074**
State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

7501 Wisconsin Avenue, Bethesda, Maryland 20814

(Address of principal executive office) (Zip Code)

Registrant s telephone number, including area code (301) 986-6200

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 requirement for the past 90 days. YES x NO ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES ¨ NO ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer, large accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	¨

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

Number of shares of common stock, par value $0.01 per share outstanding as of November 9, 2009: 18,012,000.

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SAUL CENTERS, INC.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments necessary for the fair presentation of the financial position and results of operations of Saul Centers, Inc. for the interim periods have been included. All such adjustments are of a normal recurring nature. These consolidated financial statements and the accompanying notes should be read in conjunction with the audited consolidated financial statements of Saul Centers, Inc. for the year ended December 31, 2008, which are included in its Annual Report on Form 10-K. The results of operations for interim periods are not necessarily indicative of results to be expected for the year.

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Saul Centers, Inc.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per share amounts)	**September 30, 2009 (Unaudited)**	**December 31, 2008**
Assets		
Real estate investments		
Land	$ 223,035	$ 215,407
Buildings and equipment	738,125	713,154
Construction in progress	126,066	98,920
	1,087,226	1,027,481
Accumulated depreciation	(270,413)	(252,763)
	816,813	774,718
Cash and cash equivalents	14,297	13,006
Accounts receivable and accrued income, net	36,815	37,495
Deferred leasing costs, net	16,170	16,901
Prepaid expenses, net	4,860	2,981
Deferred debt costs, net	7,466	5,875
Other assets	8,294	2,897
Total assets	$ 904,715	$ 853,873
Liabilities		
Mortgage notes payable	$ 569,634	$ 548,265
Construction loans payable	48,294	19,230
Dividends and distributions payable	12,179	12,864
Accounts payable, accrued expenses and other liabilities	27,295	22,394
Deferred income	24,015	23,233
Total liabilities	681,417	625,986
Stockholders equity		
Preferred stock, 1,000,000 shares authorized:		
Series A Cumulative Redeemable, 40,000 shares issued and outstanding	100,000	100,000
Series B Cumulative Redeemable, 31,731 shares issued and outstanding	79,328	79,328
Common stock, $0.01 par value, 30,000,000 shares authorized, 17,896,010 and 17,863,214 shares issued and outstanding, respectively	179	179
Additional paid-in capital	165,794	164,278
Accumulated deficit	(123,541)	(118,865)
Total Saul Centers, Inc. stockholders equity	221,760	224,920
Noncontrolling interest	1,538	2,967
Total stockholders equity	223,298	227,887

Total liabilities and stockholders equity	$ 904,715	$ 853,873

The accompanying notes are an integral part of these statements

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Saul Centers, Inc.

CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(Dollars in thousands, except per share amounts)	For The Three Months Ended September 30, 2009	2008	For The Nine Months Ended September 30, 2009	2008
Revenue				
Base rent	$ 31,776	$ 31,466	$ 93,572	$ 93,599
Expense recoveries	7,145	7,652	21,773	21,730
Percentage rent	214	253	775	799
Other	1,138	1,576	3,258	3,646
Total revenue	40,273	40,947	119,378	119,774
Operating expenses				
Property operating expenses	4,919	5,360	15,134	14,872
Provision for credit losses	189	236	748	660
Real estate taxes	4,531	4,241	13,567	12,530
Interest expense and amortization of deferred debt costs	8,942	8,568	25,920	25,877
Depreciation and amortization of deferred leasing costs	7,084	8,487	21,208	22,419
General and administrative	3,259	2,791	9,328	8,904
Total operating expenses	28,924	29,683	85,905	85,262
Operating income	11,349	11,264	33,473	34,512
Loss on early extinguishment of debt			(1,660)	
Gain on property dispositions				205
Net income	11,349	11,264	31,813	34,717
Noncontrolling interest				
Income attributable to the noncontrolling interest	(1,742)	(1,743)	(4,746)	(5,837)
Net income attributable to Saul Centers, Inc.	9,607	9,521	27,067	28,880
Preferred dividends	(3,785)	(3,785)	(11,355)	(9,668)
Net income available to common stockholders	$ 5,822	$ 5,736	$ 15,712	$ 19,212
Per share net income available to common stockholders				
Basic	$ 0.33	$ 0.32	$ 0.88	$ 1.08
Diluted	$ 0.32	$ 0.32	$ 0.88	$ 1.07
Dividends declared per common share outstanding	$ 0.36	$ 0.47	$ 1.14	$ 1.41

The accompanying notes are an integral part of these statements

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Saul Centers, Inc.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

(Unaudited)

(Dollars in thousands, except per share amounts)	Preferred Stock	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Total Saul Centers, Inc.	Noncontrolling Interest	Total
Stockholders equity:							
Balance, December 31, 2008	$ 179,328	$ 179	$ 164,278	$ (118,865)	$ 224,920	$ 2,967	$ 227,887
Issuance of 9,146 shares of common stock:							
7,485 shares due to dividend reinvestment plan			243		243		243
1,661 shares due to employee stock options and directors deferred stock plan and stock option awards			165		165		165
Net income				9,741	9,741	1,809	11,550
Distributions payable preferred stock:							
Series A, $50.00 per share				(2,000)	(2,000)		(2,000)
Series B, $56.25 per share				(1,785)	(1,785)		(1,785)
Distributions payable common stock ($0.39/share) and distributions payable partnership units ($0.39/share)				(6,970)	(6,970)	(2,112)	(9,082)
Balance, March 31, 2009	179,328	179	164,686	(119,879)	224,314	2,664	226,978
Issuance of 12,479 shares of common stock:							
7,324 shares due to dividend reinvestment plan			229		229		229
5,155 shares due to employee stock options and directors deferred stock plan and stock option awards			452		452		452
Net income				7,719	7,719	1,195	8,914
Distributions payable preferred stock:							
Series A, $50.00 per share				(2,000)	(2,000)		(2,000)
Series B, $56.25 per share				(1,785)	(1,785)		(1,785)
Distributions payable common stock ($0.39/share) and distributions payable partnership units ($0.39/share)				(6,975)	(6,975)	(2,112)	(9,087)
Balance, June 30, 2009	179,328	179	165,367	(122,920)	221,954	1,747	223,701
Issuance of 11,171 shares of common stock:							
6,995 shares due to dividend reinvestment plan			231		231		231
4,176 shares due to employee stock options and directors deferred stock plan and stock option awards			196		196		196
Net income				9,607	9,607	1,742	11,349
Distributions payable preferred stock:							
Series A, $50.00 per share				(2,000)	(2,000)		(2,000)
Series B, $56.25 per share				(1,785)	(1,785)		(1,785)
Distributions payable common stock ($0.36/share) and distributions payable partnership units ($0.36/share)				(6,443)	(6,443)	(1,951)	(8,394)
Balance, September 30, 2009	$ 179,328	$ 179	$ 165,794	$ (123,541)	$ 221,760	$ 1,538	$ 223,298

The accompanying notes are an integral part of these statements

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Saul Centers, Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(Dollars in thousands)	For The Nine Months Ended September 30, 2009	2008
Cash flows from operating activities:		
Net income	$ 31,813	$ 34,717
Adjustments to reconcile net income to net cash provided by operating activities:		
Gain on property dispositions		(205)
Depreciation and amortization of deferred leasing costs	21,208	22,419
Amortization of deferred debt costs	1,538	889
Non cash compensation costs from stock grants and options	767	954
Provision for credit losses	748	660
Decrease (increase) in accounts receivable and accrued income	(55)	(2,366)
Increase in deferred leasing costs	(2,655)	(1,625)
Increase in prepaid expenses	(1,879)	(2,071)
(Increase) decrease in other assets	(5,397)	457
Increase in accounts payable, accrued expenses and other liabilities	3,505	2,561
Increase in deferred income	782	919
Net cash provided by operating activities	50,375	57,309
Cash flows from investing activities:		
Acquisitions of real estate investments, net (1)		(63,406)
Additions to real estate investments	(6,185)	(6,998)
Additions to development and redevelopment activities	(52,349)	(31,546)
Proceeds from property dispositions		205
Net cash used in investing activities	(58,534)	(101,745)
Cash flows from financing activities:		
Proceeds from mortgage notes payable	86,882	44,876
Repayments on mortgage notes payable	(65,513)	(12,271)
Proceeds from construction loans payable	29,064	
Proceeds from revolving credit facility	30,000	19,000
Repayments on revolving credit facility	(30,000)	(27,000)
Additions to deferred debt costs	(3,129)	(773)
Proceeds from the issuance of:		
Series B preferred stock, net of issuance costs		76,317
Common stock	749	4,255
Distributions to:		
Series A preferred stockholders	(6,000)	(6,000)
Series B preferred stockholders	(5,355)	(1,883)
Common stockholders	(20,911)	(25,075)
Noncontrolling interest	(6,337)	(7,638)
Net cash provided by financing activities	9,450	63,808
Net increase in cash and cash equivalents	1,291	19,372

Cash and cash equivalents, beginning of period	13,006	5,765
Cash and cash equivalents, end of period	$ 14,297	$ 25,137

Supplemental discussion of non-cash investing and financing activities:

(1) The 2008 real estate acquisition costs of $63,406 are presented exclusive of a mortgage loan assumed of $10,349.

The accompanying notes are an integral part of these statements

Notes to Consolidated Financial Statements (Unaudited)

1. Organization, Formation and Structure

Saul Centers, Inc. (Saul Centers) was incorporated under the Maryland General Corporation Law on June 10, 1993. Saul Centers operates as a real estate investment trust (a REIT) under the Internal Revenue Code of 1986, as amended (the Code). A REIT is required to annually distribute at least 90% of its REIT taxable income (excluding net capital gains) to its stockholders and meet certain organizational and other requirements. Saul Centers has made and intends to continue to make regular quarterly distributions to its stockholders. Saul Centers, together with its wholly owned subsidiaries and the limited partnerships of which Saul Centers or one of its subsidiaries is the sole general partner, are referred to collectively as the Company. B. Francis Saul II serves as Chairman of the Board of Directors and Chief Executive Officer of Saul Centers.

Saul Centers was formed to continue and expand the shopping center business previously owned and conducted by the B.F. Saul Real Estate Investment Trust, the B.F. Saul Company, Chevy Chase Bank, F.S.B. and certain other affiliated entities, each of which, with the exception of Chevy Chase Bank, F.S.B., is currently controlled by B. Francis Saul II and his family members (collectively, The Saul Organization). On August 26, 1993, members of The Saul Organization transferred to Saul Holdings Limited Partnership, a newly formed Maryland limited partnership (the Operating Partnership), and two newly formed subsidiary limited partnerships (the Subsidiary Partnerships, and collectively with the Operating Partnership, the Partnerships), shopping center and office properties, and the management functions related to the transferred properties. Since its formation, the Company has developed and purchased additional properties.

The following table lists the properties acquired and/or developed by the Company since December 31, 2006. All of the following properties are operating shopping centers.

Name of Property	Location	Date of Acquisition/Development
Acquisitions		
Orchard Park	Dunwoody, GA	2007
Great Falls Shopping Center	Great Falls, VA	2008
BJ s Wholesale Club	Alexandria, VA	2008
Marketplace at Sea Colony	Bethany Beach, DE	2008
Developments		
Lansdowne Town Center	Leesburg, VA	2006/7
Ashland Square Phase I	Manassas, VA	2007
Northrock	Warrenton, VA	2008/9
Westview Village	Frederick, MD	2007/9

As of September 30, 2009, the Company s properties (the Current Portfolio Properties) consisted of 47 operating shopping center properties (the Shopping Centers), five predominantly office operating properties (the Office Properties) and four (non-operating) land or development properties.

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Notes to Consolidated Financial Statements (Unaudited) (Continued)

In September 1997, the Company established Saul QRS, Inc., a wholly owned subsidiary of Saul Centers, to facilitate the placement of collateralized mortgage debt. Saul QRS, Inc. was created to succeed to the interest of Saul Centers as the sole general partner of Saul Subsidiary I Limited Partnership. The remaining limited partnership interests in Saul Subsidiary I Limited Partnership and Saul Subsidiary II Limited Partnership are held by the Operating Partnership as the sole limited partner. Through this structure, the Company owns 100% of the Current Portfolio Properties.

2. Summary of Significant Accounting Policies

Nature of Operations

The Company, which conducts all of its activities through its subsidiaries, the Operating Partnership and Subsidiary Partnerships, engages in the ownership, operation, management, leasing, acquisition, renovation, expansion, development and financing of community and neighborhood shopping centers and office properties, primarily in the Washington, DC/Baltimore metropolitan area.

Because the properties are located primarily in the Washington, DC/Baltimore metropolitan area, the Company is subject to a concentration of credit risk related to these properties. A majority of the Shopping Centers are anchored by several major tenants. As of September 30, 2009, thirty-one of the Shopping Centers were anchored by a grocery store and offer primarily day-to-day necessities and services. Only three retail tenants, Giant Food (4.5%), a tenant at eight Shopping Centers, Safeway (3.4%), a tenant at eight Shopping Centers and Chevy Chase Bank (2.7%), a tenant at twenty properties, and one office tenant, the United States Government (2.9%), a tenant at six properties, individually accounted for more than 2.5% of the Company s total revenue for the nine months ended September 30, 2009.

Principles of Consolidation

The accompanying consolidated financial statements of the Company include the accounts of Saul Centers and its subsidiaries, including the Operating Partnership and Subsidiary Partnerships, which are majority owned by Saul Centers. All significant intercompany balances and transactions have been eliminated in consolidation.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with U.S. GAAP for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments necessary for the fair presentation of the financial position and results of operations of Saul Centers, Inc. for the interim periods have been included. All such adjustments are of a normal recurring nature. These consolidated financial statements and the accompanying notes should be read in conjunction with the audited consolidated financial statements of Saul Centers, Inc. for the year

Notes to Consolidated Financial Statements (Unaudited) (Continued)

ended December 31, 2008, which are included in its Annual Report on Form 10-K. The results of operations for interim periods are not necessarily indicative of results to be expected for the year.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Real Estate Investment Properties

The Company purchases real estate investment properties from time to time and allocates the purchase price to various components, such as land, buildings, and intangibles related to in-place leases and customer relationships. The purchase price is allocated based on the relative fair value of each component. The fair value of buildings is determined as if the buildings were vacant upon acquisition and subsequently leased at market rental rates. As such, the determination of fair value considers the present value of all cash flows expected to be generated from the property including an initial lease up period. The Company determines the fair value of above and below market intangibles associated with in-place leases by assessing the net effective rent and remaining term of the lease relative to market terms for similar leases at acquisition. In the case of above and below market leases, the Company considers the remaining contractual lease period and renewal periods, taking into consideration the likelihood of the tenant exercising its renewal options. The fair value of a below market lease component is recorded as deferred income and amortized as additional lease revenue over the remaining contractual lease period and any renewal option periods included in the valuation analysis. The fair value of above market lease intangibles is recorded as a deferred asset and is amortized as a reduction of lease revenue over the remaining contractual lease term. The Company determines the fair value of at-market in-place leases considering the cost of acquiring similar leases, the foregone rents associated with the lease-up period and carrying costs associated with the lease-up period. Intangible assets associated with at-market in-place leases are amortized as additional expense over the remaining contractual lease term. To the extent customer relationship intangibles are present in an acquisition, the fair value of the intangibles are amortized over the life of the customer relationship. The Company has never recorded a customer relationship intangible asset.

If there is an event or change in circumstance that indicates an impairment in the value of a real estate investment property, the Company prepares an impairment analysis to assess that the carrying value of the real estate investment property does not exceed its estimated fair value. The Company considers both quantitative and qualitative factors including recurring operating losses, significant decreases in occupancy, and significant adverse changes in legal factors and business climate. If impairment indicators are present the Company performs a comparison of the projected cash flows of the property over its remaining useful life, on an undiscounted basis, to the carrying value of that property. The Company assesses its undiscounted projected cash flows based upon estimated capitalization rates, historic operating results and market conditions that may affect the property. If such carrying value is greater than the undiscounted projected cash

Notes to Consolidated Financial Statements (Unaudited) (Continued)

flows, the Company would recognize an impairment loss equivalent to an amount required to adjust the carrying amount to its then estimated fair market value. The value of any property is sensitive to the actual results of any of the aforementioned estimated factors, either individually or taken as a whole. Should the actual results differ from management s projections, the valuation could be negatively or positively affected. The Company did not recognize an impairment loss on any of its real estate during the nine month periods ended September 30, 2009 and 2008.

Interest, real estate taxes, development-related salary costs and other carrying costs are capitalized on projects under development and construction. Once construction is substantially completed and the assets are placed in service, their rental income, real estate tax expense, property operating expenses (consisting of payroll, repairs and maintenance, utilities, insurance and other property related expenses) and depreciation are included in current operations. Property operating expenses are charged to operations as incurred. Interest expense capitalized totaled approximately $4,350,000 and approximately $2,876,000, for the nine month periods ended September 30, 2009 and 2008, respectively. A project is considered substantially complete and available for occupancy upon completion of tenant improvements, but no later than one year from the cessation of major construction activity. Substantially completed portions of a project are accounted for as separate projects.

Depreciation is calculated using the straight-line method and estimated useful lives of 35 to 50 years for base buildings and up to 20 years for certain other improvements that extend the useful lives. In addition, we capitalize leasehold improvements when certain criteria are met, including when we supervise construction and will own the improvements. Tenant improvements are amortized, over the shorter of the lives of the related leases or the useful life of the improvements, using the straight-line method. The depreciation component included in depreciation and amortization expense in the consolidated statements of operations, totaled approximately $17,822,000 and $18,811,000, for the nine month periods ended September 30, 2009 and 2008, respectively. Repair and maintenance expense, included in property operating expenses for the nine month periods ended September 30, 2009 and 2008, was approximately $6,736,000 and $6,835,000, respectively.

Deferred Leasing Costs

Certain initial direct costs incurred by the Company in negotiating and consummating a successful lease are capitalized and amortized over the initial base term of the lease. In addition, deferred leasing costs include amounts attributed to in place leases associated with acquisition properties. These costs are amortized over the remaining initial term of the leases acquired. Collectively, these deferred leasing costs total approximately $16,170,000 and $16,901,000, net of accumulated amortization of approximately $14,787,000 and $15,196,000, as of September 30, 2009 and December 31, 2008, respectively. Amortization expense, included in depreciation and amortization in the consolidated statements of operations, totaled approximately $3,386,000 and $3,608,000, for the nine months ended September 30, 2009 and 2008, respectively. Deferred leasing costs consist of commissions paid to third-party leasing agents as well as internal direct costs such as employee compensation and payroll-related fringe benefits directly related to time spent performing leasing-related activities for successful leases. Such activities include evaluating the prospective tenant s financial condition, evaluating and recording guarantees, collateral and other security arrangements, negotiating lease terms, preparing lease documents

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Notes to Consolidated Financial Statements (Unaudited) (Continued)

and closing the transaction. The carrying amount of these costs is written-off to expense if the applicable lease is terminated prior to expiration of the initial lease term.

Construction In Progress

Construction in progress includes preconstruction costs and development costs of active projects. Preconstruction costs associated with these active projects include legal, zoning and permitting costs and other project carrying costs incurred prior to the commencement of construction. Development costs include direct construction costs and indirect costs incurred subsequent to the start of construction such as architectural, engineering, construction management and carrying costs consisting of interest, real estate taxes and insurance. Construction in progress balances as of September 30, 2009 and December 31, 2008 are as follows:

Construction in Progress

(Dollars in thousands)	**September 30, 2009**	**December 31, 2008**
Clarendon Center	$ 94,134	$ 49,836
Northrock	11,413	21,656
Westview Village	18,892	17,240
Smallwood Village Center		6,290
Boulevard	573	2,925
Other	1,054	973
Total	$ 126,066	$ 98,920

As of September 30, 2009, 79% of the Boulevard redevelopment s leasable area had been placed in operation (approximately 6,300 square feet of space). The redevelopment costs related to the area in operation have been reclassified to land and buildings. The costs reported in Construction in Progress above reflect the costs incurred as of September 30, 2009 and December 31, 2008 for the remaining 21% and 100% of the leasable area, respectively. As of September 30, 2009, 64% of the Northrock development s leasable area had been placed in operation (approximately 64,000 square feet of space). The development costs related to the area in operation have been reclassified to land and buildings. The costs reported in Construction in Progress above reflect the costs incurred as of September 30, 2009 and December 31, 2008 for the remaining 36% and 100% of the leasable area, respectively. As of September 30, 2009, 11% of the Westview Village development s leasable area had been placed in operation (approximately 12,000 square feet of space). The development costs related to the area in operation have been reclassified to land and buildings. The costs reported in Construction in Progress above reflect the costs incurred as of September 30, 2009 and December 31, 2008 for the remaining 89% and 100% of the leasable area, respectively.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

Accounts Receivable, Accrued Income and Allowance for Doubtful Accounts

Accounts receivable primarily represent amounts currently due from tenants in accordance with the terms of the respective leases. Receivables are reviewed monthly and when, in the opinion of management, collection of the entire receivable is doubtful, revenue accrual is discontinued and an allowance for doubtful accounts is established. Accounts receivable in the accompanying financial statements are shown net of an allowance for doubtful accounts of approximately $1,152,000 and $914,000, at September 30, 2009 and December 31, 2008, respectively.

In addition to amounts due currently, accounts receivable includes accrued income of approximately $26,538,000 and $25,766,000, at September 30, 2009 and December 31, 2008, respectively, representing the cumulative difference between minimum rental income recognized on a straight-line basis and contractual payments due under the terms of respective tenant leases. These amounts are presented after netting allowances of approximately $33,000 and $51,000, respectively, for tenants whose rent payment history or financial condition casts doubt upon the tenant s ability to perform under its lease obligations.

Cash and Cash Equivalents

Cash and cash equivalents include short-term investments. Short-term investments are highly liquid investments that are both readily convertible to cash or so near their maturity that they present insignificant risk of changes in value arising from interest rate fluctuations. Short-term investments include money market accounts and other investments which generally mature within three months, measured from the acquisition date. The Company s September 30, 2009 cash balances are held in non-interest bearing accounts, which are fully insured by the Federal Government.

Deferred Debt Costs

Deferred debt costs consist of fees and costs incurred to obtain long-term financing, construction financing and the revolving line of credit. These fees and costs are capitalized and amortized on a straight-line basis over the terms of the respective loans or agreements, which approximates the effective interest method. Deferred debt costs in the accompanying financial statements are shown net of accumulated amortization of approximately $5,251,000 and $5,079,000, at September 30, 2009 and December 31, 2008, respectively.

Deferred Income

Deferred income consists of payments received from tenants prior to the time they are earned and recognized by the Company as revenue. These payments include prepayment of the following month s rent, prepayment of real estate taxes when the taxing jurisdiction has a fiscal year differing from the calendar year reimbursements specified in the lease agreement and advance payments by tenants for tenant construction work provided by the Company. In addition, deferred income includes the fair value of certain below market leases.

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Notes to Consolidated Financial Statements (Unaudited) (Continued)

Revenue Recognition

Rental and interest income is accrued as earned except when doubt exists as to collectability, in which case the accrual is discontinued. Recognition of rental income commences when control of the space has been given to the tenant. When rental payments due under leases vary from a straight-line basis because of free rent periods or scheduled rent increases, income is recognized on a straight-line basis throughout the initial term of the lease. Expense recoveries represent a portion of property operating expenses billed to tenants, including common area maintenance, real estate taxes and other recoverable costs. Expense recoveries are recognized in the period when the expenses are incurred. Rental income based on a tenant s revenues, known as percentage rent, is accrued when a tenant reports sales that exceed a specified breakpoint, pursuant to the terms of their respective leases.

Income Taxes

The Company made an election to be treated, and intends to continue operating so as to qualify as a REIT under the Code, commencing with its taxable year ended December 31, 1993. A REIT generally will not be subject to federal income taxation, provided that distributions to its stockholders equal or exceed it s REIT taxable income and complies with certain other requirements. Therefore, no provision has been made for federal income taxes in the accompanying consolidated financial statements.

Stock-based Employee Compensation, Deferred Compensation and Stock Plan for Directors

Effective January 2003, the Company adopted the fair value method to value and account for employee stock options using the prospective transition method. The Company had no options eligible for valuation prior to the grant of options in 2003. The fair value of options granted is determined at the time of each award using the Black-Scholes model, a widely used method for valuing stock-based employee compensation, and the following assumptions: (1) Expected Volatility expected volatility is determined using the most recent trading history of the Company s common stock (month-end closing prices) corresponding to the average expected term of the options; (2) Average Expected Term options are assumed to be outstanding for a term calculated considering prior exercise history, scheduled vesting and the expiration date; (3) Expected Dividend Yield a value management determines after considering the Company s current and historic dividend yield rates, the Company s yield in relation to other retail REITs and the Company s market yield at the grant date; and (4) Risk-free Interest Rate based upon the market yields of US Treasury obligations with maturities corresponding to the average expected term of the options at the grant date. The Company amortizes the value of options granted, ratably over the vesting period, and includes the amounts as compensation in general and administrative expenses.

The Company established a stock option plan in 1993 (the 1993 Plan) for the purpose of attracting and retaining executive officers and other key personnel. The 1993 Plan provided for grants of options to purchase a specified number of shares of common stock. A total of 400,000 shares were made available under the 1993 Plan. The 1993 Plan authorized the Compensation Committee of the Board of Directors to grant options at an exercise price not less

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Notes to Consolidated Financial Statements (Unaudited) (Continued)

than the market value of the common stock on the date the option is granted. Following a May 23, 2003 grant of shares, no additional shares remained for issuance under the 1993 Plan.

At the annual meeting of the Company s stockholders in 2004, the stockholders approved the adoption of the 2004 stock plan (the 2004 Plan) for the purpose of attracting and retaining executive officers, directors and other key personnel. The 2004 Plan, as amended in 2008, provides for grants of options to purchase up to 1,000,000 shares of common stock as well as grants of up to 200,000 shares of common stock to directors. The 2004 Plan authorizes the Compensation Committee of the Board of Directors to grant options at an exercise price which may not be less than the market value of the common stock on the date the option is granted.

Pursuant to the 2004 Plan, the Compensation Committee established a Deferred Compensation Plan for Directors for the benefit of its directors and their beneficiaries. The 2004 Plan replaced the Company s previous Deferred Compensation and Stock Plan for Directors. A director may elect to defer all or part of his or her director s fees and has the option to have the fees paid in cash, in shares of common stock or in a combination of cash and shares of common stock upon termination from the Board. If the director elects to have fees paid in stock, fees earned during a calendar quarter are aggregated and divided by the common stock s closing market price on the first trading day of the following quarter to determine the number of shares to be allocated to the director. As of September 30, 2009, 215,000 shares had been credited to the directors pursuant to the deferred compensation plans.

The Compensation Committee has also approved an annual award of shares of the Company s common stock as additional compensation to each director serving on the Board of Directors as of the record date for the Annual Meeting of Stockholders. The shares are awarded as of each Annual Meeting of Shareholders, and their issuance may not be deferred. Each director was issued 200 shares as of the 2009 Annual Meeting of Shareholders. The shares were valued at the closing stock price on the dates the shares were awarded and the total value is included in general and administrative expenses upon grant date.

Noncontrolling Interest

Saul Centers is the sole general partner of the Operating Partnership, owning a 76.7% common interest as of September 30, 2009. Noncontrolling interest in the Operating Partnership is comprised of limited partnership units owned by The Saul Organization. Noncontrolling interest as reflected on the accompanying consolidated balance sheets is increased for earnings allocated to limited partnership interests and distributions reinvested in additional units, and is decreased for limited partner distributions. Noncontrolling interest as reflected on the consolidated statements of operations represent earnings allocated to limited partnership interests held by the Saul Organization.

Per Share Data

Per share data for net income (basic and diluted) is computed using weighted average shares of common stock. Convertible limited partnership units and employee stock options are the Company s potentially dilutive securities. For all periods presented, the convertible limited partnership units are non-dilutive. Options granted in 2003 and 2004 are dilutive because the average share price of the Company s common stock exceeds the exercise prices. Options

Notes to Consolidated Financial Statements (Unaudited) (Continued)

granted 2005-2009 (332,500 options) are excluded because the average price of the Company s common stock was below the exercise prices as of September 30, 2009 and thus are non-dilutive. The treasury stock method was used to measure the effect of the dilution.

Basic and Diluted Shares Outstanding

(In thousands)	Quarter ended September 30, 2009	Quarter ended September 30, 2008	Nine months ended September 30, 2009	Nine months ended September 30, 2008
Weighted average common shares outstanding-Basic	17,892	17,834	17,881	17,801
Effect of dilutive options	47	157	37	170
Weighted average common shares outstanding-Diluted	17,939	17,991	17,918	17,971

Reclassifications

Certain reclassifications have been made to the prior year financial statements to conform to the current year presentation. The reclassifications have no impact on operating results previously reported.

Legal Contingencies

The Company is subject to various legal proceedings and claims that arise in the ordinary course of business. These matters are generally covered by insurance. Once it has been determined that a loss is probable to occur, the estimated amount of the loss is recorded in the financial statements.

New Accounting Standards

The Company adopted provisions of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Consolidation Topic on January 1, 2009. These provisions of the Consolidation Topic establish new accounting and reporting requirements for a noncontrolling (or minority) interest in a subsidiary and for the deconsolidation of a subsidiary. Specifically, these provisions require (i) the reclassification of minority interest in the consolidated balance sheets of the Company to noncontrolling interest, a component of permanent equity, (ii) the reclassification of minority interest expense to net income attributable to noncontrolling interest on the consolidated statements of operations, (iii) the inclusion of noncontrolling interest in the statement of stockholders equity, and (iv) additional disclosures, including noncontrolling interest activity for the quarter and nine months ended September 30, 2009 and 2008. Adoption of these provisions in the Consolidation Topic did not have a material impact on the Company s reported consolidated financial position, results of operations or cash flows.

The Company adopted provisions of the ASC Business Combinations Topic on January 1, 2009. These provisions require most identifiable assets and liabilities acquired in a business combination be recorded at full fair value . Transaction costs are no longer included in the

Notes to Consolidated Financial Statements (Unaudited) (Continued)

measurement of the business acquired. Instead, these items are expensed as incurred. These provisions apply prospectively to business combinations.

In the second quarter of 2009, the Company adopted provisions of the ASC Subsequent Events Topic. These provisions establish general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued.

3. Real Estate Acquired

Westview Village

In November 2007, the Company purchased a land parcel in the Westview development on Buckeystown Pike (MD Route 85) in Frederick, Maryland. The purchase price was $5.0 million. Construction of the building shell was completed in the second quarter of 2009, and the project s initial tenants have opened for business.

Northrock

In January 2008, the Company acquired an undeveloped land parcel in Warrenton, Virginia, located at the southwest corner of the U.S. Route 29/211 and Fletcher Drive intersection. The land purchase price was $12.5 million. The Company has substantially completed construction of a neighborhood shopping center, and the Harris Teeter supermarket and one pad building tenant have commenced operations.

Great Falls Center

On March 28, 2008, the Company completed the acquisition of the Safeway-anchored Great Falls Center located in Great Falls, Virginia. The center was acquired for a purchase price of $36.6 million subject to the assumption of a $10.3 million mortgage loan. As of the date of acquisition, management determined the mortgage loan was fairly valued because the terms of the loan were not materially different from market terms.

BJ s Wholesale Club

On March 28, 2008, the Company completed the acquisition of the single tenant property anchored by BJ s Wholesale Club, located in Alexandria, Virginia. The property was acquired for a purchase price of $21.0 million.

Marketplace at Sea Colony

On March 28, 2008, the Company completed the acquisition of Marketplace at Sea Colony, located in Bethany Beach, Delaware. The center was acquired for a purchase price of $3.0 million.

4. Noncontrolling Interest - Holders of Convertible Limited Partnership Units in the Operating Partnership

The Saul Organization has a 23.3% limited partnership interest, represented by approximately 5,416,000 convertible limited partnership units, in the Operating Partnership, as of September 30, 2009. These convertible limited partnership units are convertible into shares of

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Notes to Consolidated Financial Statements (Unaudited) (Continued)

Saul Centers common stock, at the option of the unit holder, on a one-for-one basis provided that, in accordance with the Saul Centers, Inc. Articles of Incorporation, the rights may not be exercised at any time that The Saul Organization beneficially owns, directly or indirectly, in the aggregate more than 39.9% of the value of the outstanding common stock and preferred stock of Saul Centers (the Equity Securities). As of September 30, 2009, all 5,416,000 units were convertible into shares of Saul Centers common stock.

The impact of The Saul Organization s approximately 23.3% limited partnership interest in the Operating Partnership is reflected as Noncontrolling Interest in the accompanying consolidated financial statements. Fully converted partnership units and diluted weighted average shares outstanding for the quarter ended September 30, 2009 and 2008, were approximately 23,355,000 and 23,407,000, respectively, and for the nine months ended September 30, 2009 and 2008, were approximately 23,334,000 and 23,387,000, respectively.

Noncontrolling Interest

	Quarter ended September 30,		Nine months ended September 30,	
(In thousands)	**2009**	**2008**	**2009**	**2008**
Beginning balance	$ 1,747	$ 3,747	$ 2,967	$ 4,745
Income allocation	1,742	1,743	4,746	5,837
Distributions	(1,951)	(2,546)	(6,175)	(7,638)
Ending balance	$ 1,538	$ 2,944	$ 1,538	$ 2,944

5. Mortgage Notes Payable, Revolving Credit Facility, Interest and Amortization of Deferred Debt Costs

The Company s outstanding debt totaled approximately $617,928,000 at September 30, 2009, of which approximately $569,634,000 was fixed-rate debt and approximately $48,294,000 was variable rate debt.

In addition to the outstanding indebtedness, the Company has a $150,000,000 unsecured revolving credit facility. The facility provides working capital and funds for acquisitions, certain developments and redevelopments, expires on June 30, 2012 and provides for an additional one-year extension at the Company s option, subject to the Company s satisfaction of certain conditions. Letters of credit may be issued under the revolving credit facility. As of September 30, 2009, of the $150,000,000 available for borrowing, there were no outstanding borrowings, approximately $224,000 was committed for letters of credit, and the resulting balance of approximately $149,776,000 was available to borrow for working capital, operating property acquisitions or development projects. The interest rate under the facility is primarily determined based on operating income generated by the Company s existing unencumbered properties and, to a lesser extent, certain leverage tests. As of September 30, 2009, operating income from the unencumbered properties determined the interest rate for up to $105,000,000 of the line s available borrowings, with interest expense to be calculated based upon LIBOR plus a spread of 3.65% to 3.90%. The interest rate on the remaining $45,000,000 of the line s availability is determined based upon the Company s consolidated operating income after debt service. On this

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Notes to Consolidated Financial Statements (Unaudited) (Continued)

portion of the facility, interest accrues at a rate of LIBOR plus a spread of 4.45% to 5.25%, determined by certain leverage tests. The Company may elect to use the 1, 2, 3 or 6 month LIBOR, but in no event shall LIBOR be less than 1.5%.

On April 30, 2009, the Company entered into a Modification Agreement, in effect until August 1, 2009, which reduced the Debt Service Coverage covenant under its revolving credit facility from 1.6x to 1.5x and increased the interest rate from a range of LIBOR plus 1.40% to 1.65%, with no LIBOR floor. The maximum commitment under the revolving credit facility was reduced from $150,000,000 to $120,000,000.

On July 9, 2009, the Company entered into a Second Modification Agreement to its then $120,000,000 unsecured revolving credit facility. The modification extended the maturity date of the facility from December 19, 2010 to June 30, 2012, which term may be further extended by the Company for one additional year subject to the Company s satisfaction of certain conditions. Until December 31, 2010, certain or all of the lenders may, upon request by the Company, increase the revolving credit facility line by $30,000,000. The modification reduced the interest expense coverage from 2.5x to 2.2x, reduced the existing debt service coverage from 1.5x to 1.4x (and recharacterized such test as fixed charge coverage) and created a new debt service coverage test (exclusive of preferred stock dividends) of 1.6x.

On July 28, 2009, Company entered into a Third Modification Agreement increasing the maximum commitment under the facility from $120,000,000 to $150,000,000 with the addition of a fourth lender.

Saul Centers is a guarantor of the revolving credit facility, of which the Operating Partnership is the borrower. Saul Centers is also the guarantor of 50% of the Northrock construction loan (approximately $9,305,000 of the $18,609,000 outstanding at September 30, 2009) and the Clarendon Center construction loan (approximately $29,685,000 outstanding at September 30, 2009). The fixed-rate notes payable are all non-recourse debt except for $3,882,000 of the Great Falls Center mortgage, which is guaranteed by Saul Centers.

On May 14, 2009, the Company closed on the final portion of its April 2008 forward commitment secured by the Great Falls Center. The additional funding totaled $1,882,000 which was based upon the achievement of certain leasing requirements. The loan matures February 1, 2024, requires equal monthly principal and interest payments of $12,518, based upon a 7.00% interest rate and 30-year principal amortization, and requires a final principal payment of approximately $1,414,000 at maturity.

Also during May and June 2009, the Company refinanced the mortgage debt secured by four properties. The Company replaced mortgage debt, due to mature December 2011, with new 15-year fixed-rate mortgage debt. The amount borrowed on the new loans totaled $85,000,000 and replaced balances outstanding of $48,059,000. Because the refinanced properties were included in a cross-collateralized pool of six properties, the Company was required to pay down outstanding debt balances of two remaining properties in the amount of $4,806,000. Terms of the new mortgage debt are as follows:

On May 28, 2009, the Company closed on a new 15-year, fixed-rate mortgage loan in the amount of $16,000,000, secured by Village Center. The loan matures June 1, 2024, requires

Notes to Consolidated Financial Statements (Unaudited) (Continued)

equal monthly principal and interest payments of $119,282, based upon a 7.6% interest rate and 25-year principal amortization, and requires a final principal payment of approximately $10,060,000 at maturity.

On June 2, 2009, the Company closed on a new 15-year, fixed-rate mortgage loan in the amount of $18,500,000, secured by Leesburg Pike. The loan matures June 1, 2024, requires equal monthly principal and interest payments of $134,913, based upon a 7.35% interest rate and 25-year principal amortization, and requires a final principal payment of approximately $11,506,000 at maturity.

On June 12, 2009, the Company closed on a new 15-year, fixed-rate mortgage loan in the amount of $17,000,000, secured by Van Ness Square. The loan matures July 1, 2024, requires equal monthly principal and interest payments of $132,450, based upon an 8.11% interest rate and 25-year principal amortization, and requires a final principal payment of approximately $11,453,000 at maturity. A portion of the loan proceeds are held in escrow by the lender to fund up to $1,500,000 of future tenant improvements and leasing commissions. Additional loan proceeds of $1,564,000 are also held in a second escrow to be released pending the achievement of certain annualized base rent levels. The escrows are classified as other assets on the Consolidated Balance Sheets.

On June 19, 2009, the Company closed on a new 15-year, fixed-rate mortgage loan in the amount of $33,500,000, secured by Avenel Business Park. The loan matures July 1, 2024, requires equal monthly principal and interest payments of $246,474, based upon a 7.45% interest rate and 25-year principal amortization, and requires a final principal payment of approximately $20,926,000 at maturity.

In May 2008, the Company closed on a $21,822,000 secured construction loan, to fund the development of Northrock shopping center in Warrenton, Virginia. Funding in the amount of approximately $6,495,000 occurred at closing. The loan accrues interest at a variable interest rate of LIBOR plus 3.0% with a LIBOR minimum of 1.5%. The loan matures on May 1, 2011, with one 2-year extension option, exercisable at the Company s election subject to completion of improvements and certain debt service coverage requirements. The loan was 100% guaranteed by the Company until such time as the construction was completed, at which time the guarantee was reduced to 50% of the total principal outstanding. Approximately $18,609,000 was outstanding as of September 30, 2009, therefore $9,305,000 was guaranteed by the Company. Concurrent with the execution of the April 30, 2009 revolving credit facility modification agreement, the Company and its lender modified the terms of the construction loan for a 90-day period, to reflect a similar change to the debt service coverage covenant. Additionally, the pricing of the loan was changed to accrue interest at a variable rate of LIBOR plus 1.6%, with no LIBOR minimum.

Also in May 2008, the Company closed a $157,500,000 secured construction loan to finance the development of Clarendon Center, a mixed-use development adjacent to the Clarendon Metro station in Arlington, Virginia. The Company has guaranteed the loan, with the guarantee to be reduced subject to certain conditions related to pre-leasing, completion of construction and net operating income from the project. The loan accrues interest at a variable rate of LIBOR plus 2.5% and matures on November 14, 2011, which term may be extended by

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Notes to Consolidated Financial Statements (Unaudited)   (Continued)

the Company for two additional 9-month periods, subject to the satisfaction of certain conditions. Approximately $29,685,000 was outstanding as of September 30, 2009.

At December 31, 2008, the Company s outstanding debt totaled approximately $567,495,000, of which approximately $548,265,000 was fixed rate and $19,230,000 was variable rate debt. No balances were outstanding on the Company s $150,000,000 unsecured revolving credit facility as of December 31, 2008.

At September 30, 2009, the scheduled maturities of all debt, including scheduled principal amortization, for years ending December 31, were as follows:

Debt Maturity Schedule

(Dollars in thousands)	Balloon Payments	Scheduled Principal Amortization	Total
October 1 through December 31, 2009	$	$ 4,062	$ 4,062
2010		16,927	16,927
2011	67,553(a)	17,847	85,400
2012	96,300	16,474	112,774
2013	39,440	10,809	50,249
2014	13,176	10,713	23,889
Thereafter	247,753	76,874	324,627
	$ 464,222	$ 153,706	$ 617,928

(a) Includes the Clarendon Center and Northrock construction loan balances as of September 30, 2009, totaling $48,294.

Interest expense and amortization of deferred debt costs for the quarters and nine month periods ended September 30, 2009 and 2008, were as follows:

Interest Expense and Amortization of Deferred Debt Costs

	Quarter ended September 30,		Nine months ended September 30,	
(Dollars in thousands)	2009	2008	2009	2008
Interest incurred	$ 9,974	$ 9,454	$ 28,950	$ 27,864
Amortization of deferred debt costs	366	304	957	889
Costs related to modification of revolving credit facility	83		363	
Capitalized interest	(1,481)	(1,190)	(4,350)	(2,876)
	$ 8,942	$ 8,568	$ 25,920	$ 25,877

Notes to Consolidated Financial Statements (Unaudited) (Continued)

6. Stockholders Equity and Noncontrolling Interest

The consolidated statements of operations include net income attributable to noncontrolling interest of $4,746,000 and $5,837,000 for the nine months ended September 30, 2009 and 2008, respectively, representing The Saul Organization s limited partnership interest share of net income for each period.

On March 20, 2008, the Company filed a shelf registration statement (the Shelf Registration Statement) with the SEC relating to the future offering of up to an aggregate of $140,000,000 of preferred stock and depositary shares. On March 27, 2008, the Company sold 3,000,000 depositary shares, each representing 1/100th of a share of 9% Series B Cumulative Redeemable Preferred Stock, providing net cash proceeds of $72,100,000. The underwriters exercised an over-allotment option, purchasing an additional 173,115 depositary shares providing additional net cash proceeds of $4,200,000.

The depositary shares may be redeemed, in whole or in part, at the $25.00 liquidation preference at the Company s option on or after March 15, 2013. The depositary shares pay an annual dividend of $2.25 per share, equivalent to 9% of the $25.00 liquidation preference. The Series B preferred stock has no stated maturity, is not subject to any sinking fund or mandatory redemption and is not convertible into any other securities of the Company. Investors in the depositary shares generally have no voting rights, but will have limited voting rights if the Company fails to pay dividends for six or more quarters (whether or not declared or consecutive) and in certain other events.

7. Related Party Transactions

Chevy Chase Bank was an affiliate of The Saul Organization until February 28, 2009 and leases space in 20 of the Company s properties. Total rental income from Chevy Chase Bank amounted to approximately $658,000 for the two months ended February 28, 2009 and $2,558,000 for the nine months ended September 30, 2008.

The Chairman and Chief Executive Officer, the President, the Senior Vice President- General Counsel and the Senior Vice President-Chief Accounting Officer of the Company are also officers of various members of The Saul Organization and their management time is shared with The Saul Organization. Their annual compensation is fixed by the Compensation Committee of the Board of Directors, with the exception of the Senior Vice President-Chief Accounting Officer whose share of annual compensation allocated to the Company is determined by the shared services agreement (described below).

The Company participates in a multiemployer profit sharing retirement plan with other entities within The Saul Organization which covers those full-time employees who meet the requirements as specified in the plan. From January 1, 2002 until December 31, 2008, only employer contributions were made to the plan. Beginning January 1, 2009, all employer contributions were made to individual 401(K) accounts. Each participant who is entitled to be credited with at least one hour of service on or after January 1, 2002, is 100% vested in his or her employer contribution account and no portion of such account shall be forfeitable. Employer contributions, at the discretionary amount of up to six percent of the employee s cash

Notes to Consolidated Financial Statements (Unaudited) (Continued)

compensation, subject to certain limits, were $339,000 and $298,000, for the nine months ended September 30, 2009 and 2008, respectively. There are no past service costs associated with the plan since it is of the defined-contribution type.

The Company also participates in a multiemployer nonqualified deferred compensation plan with entities in The Saul Organization which covers those full-time employees who meet the requirements as specified in the plan. The plan, which can be modified or discontinued at any time, requires participating employees to defer 2% of their compensation in excess of a specified amount. The Company is required to contribute three times the amount deferred by employees. The Company s contribution totaled approximately $188,000 and $96,000, for the nine months ended September 30, 2009 and 2008, respectively. All amounts deferred by employees and the Company are fully vested. The cumulative unfunded liability under this plan was approximately $1,287,000 and $1,082,000 at September 30, 2009 and December 31, 2008, respectively, and is included in accounts payable, accrued expenses and other liabilities in the consolidated balance sheets.

The Company has entered into a shared services agreement (the Agreement) with The Saul Organization that provides for the sharing of certain personnel and ancillary functions such as computer hardware, software, and support services and certain direct and indirect administrative personnel. The Agreement was not impacted by the February 28, 2009 sale of Chevy Chase Bank. The method for determining the cost of the shared services is provided for in the Agreement and depending upon the service, is based upon head count, estimates of usage or estimates of time incurred, as applicable. The terms of the Agreement and the payments made thereunder are deemed reasonable by management and are reviewed annually by the Audit Committee of the Board of Directors, which consists entirely of independent directors. Billings by The Saul Organization for the Company s share of these ancillary costs and expenses for the nine months ended September 30, 2009 and 2008, which included rental expense for the Company s headquarters lease, totaled approximately $4,151,000 and $3,945,000, respectively. The amounts are expensed when billed and are primarily reported as general and administrative expenses in these consolidated financial statements. As of September 30, 2009 and December 31, 2008, accounts payable, accrued expenses and other liabilities included approximately $362,000 and $324,000, respectively, representing amounts due to The Saul Organization for the Company s share of these ancillary costs and expenses.

The Company s corporate headquarters lease, which commenced in March 2002, is leased by a member of The Saul Organization. The 10-year lease provides for base rent escalated at 3% per year, with payment of a pro-rata share of operating expenses over a base year amount. Pursuant to the Agreement, the Company pays an allocation of total rental payments on a percentage proportionate to the number of employees employed by the Company and The Saul Organization. The Company s rent expense for the nine months ended September 30, 2009 and 2008 was approximately $682,000 and $661,000, respectively, and is included in general and administrative expense.

The B. F. Saul Insurance Agency of Maryland, Inc., a subsidiary of the B. F. Saul Company and a member of The Saul Organization, is a general insurance agency that receives commissions and fees in connection with the Company s insurance program. Such commissions and fees amounted to $182,000 and $227,000 for the nine months ended September 30, 2009 and 2008, respectively.

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8. Non-Operating Items

Loss on Early Extinguishment of Debt

In conjunction with the early repayment of four mortgage loans refinanced during May and June 2009 as described in Note 5, the Company incurred prepayment penalties of $1,442,000 and wrote-off unamortized deferred debt costs of $218,000 for a combined charge of $1,660,000.

Gain on Property Dispositions

The gain on property disposition of approximately $205,000 during the quarter ended September 30, 2008 represents proceeds from an insurance settlement for HVAC units vandalized at the Company s West Park shopping center in Oklahoma City, Oklahoma. There were no property dispositions during the nine months ended September 30, 2009.

9. Stock Option Plans

The Company has established two stock incentive plans, the 1993 plan and the 2004 plan (together, the Plans). Under the Plans, options were granted at an exercise price not less than the market value of the common stock on the date of grant and expire ten years from the date of grant. Officer options vest ratably over four years following the grant and are expensed straight-line over the vesting period. Director options vest immediately and are expensed as of the date of grant.

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Note 9. Option detail (Excel schedule)

The following table summarizes the amount and activity of each grant, the total value and variables used in the computation and the amount expensed and included in general and administrative expense in the Consolidated Statements of Operations for the nine months ended September 30, 2009:

Stock options issued

	Officers					**Directors**							
	05/23/2003	**04/26/2004**	**05/06/2005**	**04/27/2007**	**Subtotals**	**04/26/2004**	**05/06/2005**	**05/01/2006**	**04/27/2007**	**04/25/2008**	**04/24/2009**	**Subtotals**	**Grand Totals**
Grant date													
Total grant	220,000	122,500	132,500	135,000	610,000	30,000	30,000	30,000	30,000	30,000	32,500	182,500	**792,500**
Vested	212,500	115,000	121,250	67,500	516,250	30,000	30,000	30,000	30,000	30,000	32,500	182,500	**698,750**
Exercised	96,422	30,625	6,250		133,297	6,200	2,500					8,700	**141,997**
Forfeited	7,500	7,500	11,250		26,250								**26,250**
Exercisable at September 30, 2009	116,078	84,375	115,000	67,500	382,953	23,800	27,500	30,000	30,000	30,000	32,500	173,800	**556,753**
Remaining unexercised	116,078	84,375	115,000	135,000	450,453	23,800	27,500	30,000	30,000	30,000	32,500	173,800	**624,253**
Exercise price	$ 24.91	$ 25.78	$ 33.22	$ 54.17		$ 25.78	$ 33.22	$ 40.35	$ 54.17	$ 50.15	$ 32.68		