

UMH PROPERTIES, INC.
Form 10-Q
May 08, 2014

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 March 31, 2014

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

For the transition period from _____ to _____

Commission File Number 001-12690

UMH PROPERTIES, INC.

(Exact name of registrant as specified in its charter)

Maryland 22-1890929

(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) identification number)

Juniper Business Plaza, 3499 Route 9 North, Suite 3-C, Freehold, NJ 07728

(Address of Principal Executive Offices) (Zip Code)

Registrant's telephone number, including area code (732) 577-9997

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes No

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

Class	Outstanding Common Shares as of May 1, 2014
Common Stock, \$.10 par value per share	21,908,506

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UMH PROPERTIES, INC. AND SUBSIDIARIES

FORM 10-Q

FOR THE QUARTER ENDED MARCH 31, 2014

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ITEM 1 – FINANCIAL STATEMENTS**UMH PROPERTIES, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****AS OF MARCH 31, 2014 AND DECEMBER 31, 2013**

	March 31, 2014 (Unaudited)	December 31, 2013
- ASSETS -		
INVESTMENT PROPERTY AND EQUIPMENT		
Land	\$ 35,992,214	\$ 33,973,214
Site and Land Improvements	277,507,325	256,830,234
Buildings and Improvements	16,049,613	13,273,690
Rental Homes and Accessories	67,387,063	61,747,274
Total Investment Property	396,936,215	365,824,412
Equipment and Vehicles	11,344,339	11,130,719
Total Investment Property and Equipment	408,280,554	376,955,131
Accumulated Depreciation	(88,039,015)	(84,655,017)
Net Investment Property and Equipment	320,241,539	292,300,114
OTHER ASSETS		
Cash and Cash Equivalents	7,760,761	7,615,143
Securities Available for Sale	60,700,743	59,254,942
Inventory of Manufactured Homes	12,106,353	13,786,041
Notes and Other Receivables, net	26,411,677	26,019,725
Unamortized Financing Costs	2,252,603	2,128,006
Prepaid Expenses and Other Assets	873,323	1,182,850
Land Development Costs	5,792,652	5,693,153
Total Other Assets	115,898,112	115,679,860
TOTAL ASSETS	\$436,139,651	\$407,979,974

See Accompanying Notes to Consolidated Financial Statements

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UMH PROPERTIES, INC. AND SUBSIDIARIES**CONSOLIDATED BALANCE SHEETS – CONTINUED****AS OF MARCH 31, 2014 AND DECEMBER 31, 2013**

	March 31, 2014 (Unaudited)	December 31, 2013
- LIABILITIES AND SHAREHOLDERS' EQUITY -		
LIABILITIES:		
MORTGAGES PAYABLE	\$ 177,641,068	\$ 160,639,944
OTHER LIABILITIES		
Accounts Payable	1,756,806	1,628,713
Loans Payable	53,623,283	49,118,996
Accrued Liabilities and Deposits	3,832,246	3,852,799
Tenant Security Deposits	2,418,070	2,153,785
Total Other Liabilities	61,630,405	56,754,293
Total Liabilities	239,271,473	217,394,237
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY:		
Series A – 8.25% Cumulative Redeemable Preferred Stock, par value \$0.10 per share, 3,663,800 shares authorized, issued and outstanding as of March 31, 2014 and December 31, 2013, respectively	91,595,000	91,595,000
Common Stock – \$0.10 par value per share, 42,000,000 shares authorized, 21,675,375 and 20,769,892 shares issued and outstanding as of March 31, 2014 and December 31, 2013, respectively	2,167,538	2,076,989
Excess Stock - \$0.10 par value per share, 3,000,000 shares authorized; no shares issued or outstanding	-0-	-0-
Additional Paid-In Capital	104,544,659	96,504,643
Accumulated Other Comprehensive Income	4,403,327	1,076,898
Accumulated Deficit	(5,842,346)	(667,793)
Total Shareholders' Equity	196,868,178	190,585,737
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$436,139,651	\$407,979,974

See Accompanying Notes to Consolidated Financial Statements

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UMH PROPERTIES, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF INCOME (LOSS) (UNAUDITED)****FOR THE THREE MONTHS ENDED****MARCH 31, 2014 AND 2013**

	THREE MONTHS ENDED	
	2014	2013
INCOME:		
Rental and Related Income	\$14,846,776	\$11,642,186
Sales of Manufactured Homes	1,002,405	1,784,109
	15,849,181	13,426,295
Total Income		
EXPENSES:		
Community Operating Expenses	8,287,609	5,947,365
Cost of Sales of Manufactured Homes	766,379	1,522,532
Selling Expenses	720,679	508,902
General and Administrative Expenses	1,519,923	1,215,236
Franchise Taxes	84,000	66,000
Acquisition Costs	285,179	591,068
Depreciation Expense	3,437,672	2,389,854
Total Expenses	15,101,441	12,240,957
OTHER INCOME (EXPENSE):		
Interest Income	547,243	538,132
Dividend Income	1,059,465	850,793
Gain on Sales of Securities Transactions, net	508,403	3,310,028
Other Income	52,687	29,080
Interest Expense	(2,208,125)	(1,679,809)
Amortization of Financing Costs	(116,580)	(71,190)
	(156,907)	2,977,034
Total Other Income (Expense)		
Income before Loss on Sales of		
Investment Property and Equipment	590,833	4,162,372
Loss on Sales of Investment	(22,644)	(12,861)

Property and Equipment		
Net Income	568,189	4,149,511
Less: Preferred Dividend	1,889,147	1,889,147
Net Income (Loss) Attributable to		
	\$(1,320,958)	\$2,260,364
Common Shareholders		

See Accompanying Notes to Consolidated Financial Statements

UMH PROPERTIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME (LOSS) – CONTINUED (UNAUDITED)

FOR THE THREE MONTHS ENDED

MARCH 31, 2014 AND 2013

	THREE MONTHS ENDED	
	2014	2013
Basic Income Per Share:		
Net Income	\$0.03	\$0.24
Less: Preferred Dividend	0.09	0.11
Net Income (Loss) Attributable to Common		\$0.13
Shareholders	\$(0.06)	
Diluted Income Per Share:		
Net Income	\$0.03	\$0.24
Less: Preferred Dividend	0.09	0.11
Net Income (Loss) Attributable to Common		\$0.13
Shareholders	\$(0.06)	
Weighted Average Common Shares Outstanding:		
Basic	21,261,375	17,441,001
Diluted	21,307,103	17,501,510

See Accompanying Notes to Consolidated Financial Statements

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UMH PROPERTIES, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)****FOR THE THREE MONTHS ENDED****MARCH 31, 2014 AND 2013**

	THREE MONTHS ENDED	
	2014	2013
Net Income	\$568,189	\$4,149,511
Other Comprehensive Income:		
Unrealized Holding Gain Arising During the Period	3,830,344	4,933,341
Reclassification Adjustment for Net Gains		(3,310,028)
Realized in Income	(508,403)	
Change in Fair Value of Interest Rate Swap Agreements	4,488	52,099
Comprehensive Income	3,894,618	5,824,923
Less: Preferred Dividend	(1,889,147)	(1,889,147)
Comprehensive Income Attributable to		
Common Shareholders	\$2,005,471	\$3,935,776

See Accompanying Notes to Consolidated Financial Statements

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UMH PROPERTIES, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)****FOR THE THREE MONTHS ENDED****MARCH 31, 2014 AND 2013**

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	\$568,189	\$4,149,511
Non-Cash Adjustments:		
Depreciation	3,437,672	2,389,854
Amortization of Financing Costs	116,580	71,190
Stock Compensation Expense	223,797	132,580
Increase in Provision for Uncollectible Notes and Other Receivables	213,776	147,205
Gain on Sales of Securities Transactions, net	(508,403)	(3,310,028)
Loss on Sales of Investment Property and Equipment	22,644	12,861
Changes in Operating Assets and Liabilities:		
Inventory of Manufactured Homes	1,679,688	98,667
Notes and Other Receivables	(605,728)	(1,756,702)
Prepaid Expenses and Other Assets	309,527	(468,158)
Accounts Payable	128,093	104,722
Accrued Liabilities and Deposits	(16,065)	(451,141)
Tenant Security Deposits	264,285	557,884
Net Cash Provided by Operating Activities	5,834,055	1,678,445
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of Manufactured Home Communities, net of mortgages assumed	(6,837,261)	(67,500,000)
Purchase of Investment Property and Equipment	(6,564,391)	(5,534,035)
Proceeds from Sales of Assets	112,650	167,403
Additions to Land Development	(99,499)	(190,195)
Purchase of Securities Available for Sale	(1,153,766)	(2,018,694)
Proceeds from Sales of Securities Available for Sale	3,538,309	15,239,333
Net Cash Used in Investing Activities	(11,003,958)	(59,836,188)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from Mortgages, net of mortgages assumed	-0-	53,760,000
Net Proceeds on short term borrowing	4,504,287	1,700,580
Principal Payments of Mortgages and Loans	(1,111,615)	(888,874)
Financing Costs on Debt	(241,177)	(704,190)
Proceeds from Issuance of Common Stock, net of reinvestments	7,454,456	6,444,772
Preferred Dividends Paid	(1,889,147)	(1,889,147)
Common Dividends Paid, net of reinvestments	(3,401,283)	(2,814,591)
Net Cash Provided by Financing Activities	5,315,521	55,608,550
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	145,618	(2,549,193)

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CASH AND CASH EQUIVALENTS-BEGINNING OF PERIOD	7,615,143	11,035,824
CASH AND CASH EQUIVALENTS-END OF PERIOD	\$7,760,761	\$8,486,631

See Accompanying Notes to Consolidated Financial Statements

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UMH PROPERTIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2014 (UNAUDITED)

NOTE 1 – ORGANIZATION AND ACCOUNTING POLICIES

UMH Properties, Inc. (“we”, “our”, “us” or “the Company”) owns and operates eighty-two manufactured home communities containing approximately 14,500 developed home sites. The communities are located in New Jersey, New York, Ohio, Pennsylvania, Tennessee, Indiana and Michigan. The Company, through its wholly-owned taxable subsidiary, UMH Sales and Finance, Inc. (S&F), conducts manufactured home sales in its communities. S&F was established to enhance the occupancy of the communities. The consolidated financial statements of the Company include S&F and all of its other wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation. The Company also invests in securities of other Real Estate Investment Trusts (REITs).

The Company has elected to be taxed as a REIT under Sections 856-860 of the Internal Revenue Code (the Code), and intends to maintain its qualification as a REIT in the future. As a qualified REIT, with limited exceptions, the Company will not be taxed under federal and certain state income tax laws at the corporate level on taxable income that it distributes to its shareholders. For special tax provisions applicable to REITs, refer to Sections 856-860 of the Code. The Company is subject to franchise taxes in some of the states in which the Company owns property.

The interim Consolidated Financial Statements furnished herein have been prepared in accordance with accounting principles generally accepted in the United States of America (US GAAP) applicable to interim financial information, the instructions to Form 10-Q, and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by US GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three months ended March 31, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014. For further information, refer to the Consolidated Financial Statements and footnotes thereto included in the Company’s annual report on Form 10-K for the year ended December 31, 2013.

Use of Estimates

In preparing the Consolidated Financial Statements in accordance with US GAAP, management is required to make estimates and assumptions that affect the reported amounts of Assets and Liabilities, as well as contingent Assets and Liabilities as of the dates of the Consolidated Balance Sheets and Revenue and Expenses for the years then ended. Actual results could differ significantly from these estimates and assumptions.

Stock Based Compensation

The Company accounts for awards of stock options and restricted stock in accordance with ASC 718-10, Compensation-Stock Compensation. ASC 718-10 requires that compensation cost for all stock awards be calculated and amortized over the service period (generally equal to the vesting period). The compensation cost for stock option grants is determined using option pricing models, intended to estimate the fair value of the awards at the grant date less estimated forfeitures. The compensation expense for restricted stock is recognized based on the fair value of the restricted stock awards less estimated forfeitures. The fair value of restricted stock awards is equal to the fair value of the Company's stock on the grant date. Compensation costs of \$223,797 and \$132,580 have been recognized for the three months ended March 31, 2014 and 2013, respectively.

On January 15, 2014, the Company awarded to Samuel A. Landy a restricted stock award of 25,000 shares in accordance with his employment agreement. The grant date fair value of this restricted stock grant was \$232,750. This grant vests over 5 years.

As of March 31, 2014, there were options outstanding to purchase 1,043,000 shares. There were 2,593,000 shares available for grant under the 2013 Stock Option and Stock Award Plan, as amended. During the three months ended March 31, 2014, options to one employee to purchase a total of 50,000 shares expired. The aggregate intrinsic value of options outstanding as of March 31, 2014 was \$493,203. As of March 31, 2013, there were options outstanding to purchase 745,000 shares and 558,188 shares were available for grant under the Company's 2003 Stock Option and Stock Award Plan, as amended.

Derivative Instruments and Hedging Activities

In the normal course of business, the Company is exposed to financial market risks, including interest rate risk on our variable rate debt. We attempt to limit these risks by following established risk management policies, procedures and strategies, including the use of derivative financial instruments. The Company's primary strategy in entering into derivative contracts is to minimize the variability that changes in interest rates could have on its future cash flows. The Company generally employs derivative instruments that effectively convert a portion of its variable rate debt to fixed rate debt. The Company does not enter into derivative instruments for speculative purposes. The Company had entered into various interest rate swap agreements that had the effect of fixing interest rates relative to specific mortgage loans.

During 2012, the Company entered into two interest rate swap agreements that have the effect of fixing interest rates relative to specific mortgage loans as follows:

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Mortgage	Due Date	Mortgage	Effective	Balance 3/31/14
		Interest Rate	Fixed Rate	
Allentown/Clinton	2/1/2017	LIBOR + 3.25%	4.39%	\$10,721,062
Various – 11 properties	8/1/2017	LIBOR + 3.00%	3.89%	\$12,726,571

The Company's interest rate swap agreements are based upon 30-day LIBOR. The re-pricing and scheduled maturity dates, payment dates, index and the notional amounts of the interest rate swap agreements coincide with those of the underlying mortgage. The interest rate swap agreements are net settled monthly. The Company has designated these derivatives as cash flow hedges and has recorded the fair value on the balance sheet in accordance with ASC 815, Derivatives and Hedging (See Note 7 for information on the determination of fair value). The effective portion of the gain or loss on these hedges will be reported as a component of Accumulated Other Comprehensive Income in our Consolidated Balance Sheets. To the extent that the hedging relationships are not effective or do not qualify as cash flow hedges, the ineffective portion is recorded in Interest Expense. Hedges that received designated hedge accounting treatment are evaluated for effectiveness at the time that they are designated as well as through the hedging period. As of March 31, 2014 and December 31, 2013, the Company has determined that these interest rate swap agreements are highly effective as cash flow hedges. As a result, the fair value of these derivatives of \$(35,352) and \$(39,840), respectively, was recorded as a component of Accumulated Other Comprehensive Income, with the corresponding liability included in Accrued Liabilities and Deposits.

Recent Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-08, "Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity". ASU No. 2014-08 changes the definition of a discontinued operation to include only those disposals of components of an entity that represent a strategic shift that has (or will have) a major effect on an entity's operations and financial results. ASU No. 2014-08 is effective prospectively for fiscal years beginning after December 15, 2014, with earlier adoption permitted. The Company has decided to early adopt this standard effective with the interim period beginning January 1, 2014. Management believes that the adoption of ASU No. 2014-08 will not have a material impact on our financial position, results of operations or cash flows.

Management does not believe that any other recently issued, but not yet effective accounting pronouncements, if adopted, would have a material effect on the accompanying Consolidated Financial Statements.

Reclassifications

Certain amounts in the financial statements for the prior periods have been reclassified to conform to the statement presentation for the current periods.

NOTE 2 – NET INCOME (LOSS) PER SHARE

Basic Net Income (Loss) per Share is calculated by dividing Net Income (Loss) by the weighted average shares outstanding for the period. Diluted Net Income (Loss) per Share is calculated by dividing Net Income (Loss) by the weighted average number of common shares outstanding plus the weighted average number of net shares that would be issued upon exercise of stock options pursuant to the treasury stock method. Common stock equivalents resulting

from stock options in the amount of 45,728 and 60,509 shares for the three months ended March 31, 2014 and 2013, respectively, are included in the diluted weighted shares outstanding. As of March 31, 2014 and 2013, options to purchase 844,000 and 536,000 shares, respectively, were antidilutive.

NOTE 3 – INVESTMENT PROPERTY AND EQUIPMENT

On March 13, 2014, the Company acquired 8 manufactured home communities for \$24,950,000. These 8 all-age communities total 1,018 sites and are situated on approximately 270 acres. These communities are all located in Ohio. The average occupancy for these communities at closing was approximately 70%. The Company assumed mortgages totaling approximately \$18,100,000 and used its Unsecured Revolving Credit Facility with Bank of Montreal (“Credit Facility”) to finance this acquisition (see Note 5).

This acquisition has been accounted for utilizing the acquisition method of accounting in accordance with ASC 805, Business Combinations, and accordingly, the result of the acquired assets are included in the statements of operations from the dates of acquisition. The following table summarizes the estimated fair value of the assets acquired for the quarter ended March 31, 2014:

	At Acquisition Date
Assets Acquired:	
Land	\$2,019,000
Depreciable Property	22,813,147
Other	117,853
Total Assets Acquired	\$24,950,000

The purchase price allocations are preliminary and may be adjusted as final costs and valuations are determined.

NOTE 4 – SECURITIES AVAILABLE FOR SALE

The Company owns a portfolio of securities of other REITs. During the three months ended March 31, 2014, the Company sold securities with a cost of \$3,029,906 and recognized a Gain on Sale of \$508,403. The Company also made purchases of \$1,153,766 in Securities Available for Sale. Of this amount, the Company made total purchases of 31,114 common shares of Monmouth Real Estate Investment Corporation (MREIC), a related REIT, through MREIC’s Dividend Reinvestment and Stock Purchase Plan for a total cost of \$281,272 or weighted average cost of \$9.04 per share. The Company owned a total of 1,906,261 MREIC common shares as of March 31, 2014 at a total cost of \$15,772,747 and a fair value of \$18,185,726.

As of March 31, 2014, the Company had eleven securities that were temporarily impaired. The Company considers many factors in determining whether a security is other than temporarily impaired, including the nature of the security and the cause, severity and duration of

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the impairment.

The following is a summary of temporarily impaired securities at March 31, 2014:

	Less Than 12 Months		12 Months or Longer	
	Fair	Unrealized	Fair	Unrealized
	<u>Value</u>	<u>Loss</u>	<u>Value</u>	<u>Loss</u>
Preferred Stock	\$ 3,944,894	\$ (82,258)	\$ -0-	\$ -0-
Common Stock	1,783,950	(269,441)	\$ -0-	\$ -0-
Total	\$ 5,728,844	\$ (351,699)	\$ -0-	\$ -0-

The following is a summary of the range of the losses on these temporarily impaired securities:

Number of

<u>Individual Securities</u>	<u>Fair Value</u>	<u>Unrealized Loss</u>	<u>Range of Loss</u>
9	\$ 3,937,154	\$ (68,486)	0% to 5%
1	232,440	(17,560)	7%
1	1,559,250	(265,653)	15%
11	\$ 5,728,844	\$ (351,699)	

The Company has determined that these securities are temporarily impaired as of March 31, 2014. The Company normally holds REIT securities long term and has the ability and intent to hold securities to recovery. As of March 31, 2014, the Company had total net unrealized gains of \$4,438,679 in its REIT securities portfolio.

NOTE 5 – LOANS AND MORTGAGES PAYABLE

On March 13, 2014, the Company assumed approximately \$18.1 million in mortgage loans on its 8 community acquisition. The weighted average interest rate on these mortgages is fixed at 6.74%. Approximately \$8.9 million matures on May 1, 2016 and the remaining balance matures on February 1, 2018. In addition, the Company borrowed \$10.0 million on its Credit Facility to finance this acquisition.

NOTE 6 - SHAREHOLDERS' EQUITY

Common Stock

On March 17, 2014, the Company paid \$3,853,595 of which \$452,312 was reinvested, as a dividend of \$0.18 per share to common shareholders of record as of close of business on February 18, 2014.

During the three months ended March 31, 2014, the Company received, including dividends reinvested of \$452,312, a total of \$7,906,768 from its Dividend Reinvestment and Stock Purchase Plan (DRIP). There were 880,483 new shares issued under the DRIP.

On April 1, 2014, the Company declared a dividend of \$0.18 per share to be paid June 16, 2014 to common shareholders of record as of close of business on May 15, 2014.

8.25% Series A Cumulative Redeemable Preferred Stock

On March 17, 2014, the Company paid \$1,889,147 in Preferred Dividends or \$0.515625 per share for the period from December 1, 2013 through February 28, 2014 to preferred shareholders of record as of close of business on February 18, 2014. Series A preferred share dividends are cumulative and payable quarterly at an annual rate of \$2.0625 per share.

On April 1, 2014, the Company declared a Preferred Dividend of \$0.515625 per share for the period from March 1, 2014 through May 31, 2014 to be paid on June 16, 2014 to preferred shareholders of record as of close of business on May 15, 2014.

NOTE 7 - FAIR VALUE MEASUREMENTS

In accordance with ASC 820-10, Fair Value Measurements and Disclosures, the Company measures certain financial Assets and Liabilities at fair value on a recurring basis, including Securities Available for Sale. The fair value of these financial Assets and Liabilities was determined using the following inputs at March 31, 2014 and December 31, 2013:

Fair Value Measurements at Reporting Date Using

	Total	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<u>As of March 31, 2014:</u>				
Securities Available for Sale - Preferred stock	\$24,462,440	\$24,462,440	\$-0-	\$-0-
Securities Available for Sale - Common stock	36,238,303	36,238,303	-0-	-0-
Interest Rate Swap (1)	(35,352)	-0-	(35,352)	-0-
Total	\$60,665,391	\$60,700,743	\$(35,352)	\$-0-
<u>As of December 31, 2013:</u>				
Securities Available for Sale - Preferred stock	\$24,536,942	\$24,536,942	\$-0-	\$-0-
Securities Available for Sale - Common stock	34,718,000	34,718,000	-0-	-0-
Interest Rate Swap (1)	(39,840)	-0-	(39,840)	-0-

Total	\$59,215,102	\$59,254,942	\$(39,840)	\$-0-
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(1) Included in Accrued Liability and Deposits

In addition to the Company's investments in securities available for sale and interest rate swaps, the Company is required to disclose certain information about the fair values of other financial instruments, as defined in ASC 825-10, Financial Instruments. Estimates of fair value are

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made at a specific point in time, based upon, where available, relevant market prices and information about the financial instrument. Such estimates do not include any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. All of the Company's Securities Available for Sale have quoted market prices and are therefore classified in Level 1 of the fair value hierarchy. A quoted market price is indirectly available for our interest rate swap. This price is determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows, and reflects the contractual terms of the derivative, including the period to maturity, and uses observable market-based inputs. As such, we have determined that the valuation of this interest rate swap is classified in Level 2 of the fair value hierarchy.

The fair value of Cash and Cash Equivalents and Notes Receivable approximates their current carrying amounts since all such items are short-term in nature. The fair value of Variable Rate Mortgages Payable and Loans Payable approximate their current carrying amounts since such amounts payable are at approximately a weighted-average current market rate of interest. As of March 31, 2014, the fair and carrying value of Fixed Rate Mortgages Payable amounted to \$145,763,677 and \$145,960,746, respectively. The fair value of Mortgages Payable is estimated based upon discounted cash flows at current market rates for instruments with similar remaining terms.

NOTE 8 – CONTINGENCIES, COMMITMENTS AND OTHER MATTERS

From time to time, the Company may be subject to claims and litigation in the ordinary course of business. Management does not believe that any such claims or litigation have a material adverse effect on the financial position or results of operations.

In 2010, a rainstorm bringing 13 inches of rain in a two-hour period caused flooding at Memphis Mobile City. All homes owned by us were fully restored as were the homes of all residents who elected to make repairs. On May 9, 2011, we were notified that a lawsuit had been filed in the United States District Court for the Western District of Tennessee on behalf of a purported class of all individuals of Mexican national origin who are current or former residents of Memphis Mobile City. The complaint alleges various claims based on federal and state discrimination and consumer protection laws, seeking monetary damages and injunctive relief. On September 30, 2012, the magistrate judge ruled that plaintiffs who had signed a security agreement with an arbitration clause would be obligated to arbitrate while the other plaintiffs would not. The plaintiffs have filed a statement of alleged damages for each member of the purported class. Plaintiffs have been ordered to submit releases to FEMA so that we might begin to evaluate their damage claims with respect to compensation they may have already received from that federal agency. Plaintiffs' counsel notified us in July that they have filed such releases as to many of the plaintiffs. FEMA is in the process of producing their documents. On June 25, 2013, in connection with a hearing on our Motion to Dismiss, the court ordered the plaintiffs to amend their Complaint to plead their claims with specificity. Plaintiffs filed an amended Complaint containing allegations substantially similar to the initial Complaint. We filed a Motion to Dismiss the amended Complaint which plaintiffs opposed. Oral arguments on this motion took place on May 1, 2014. We are awaiting the Court's decision. We continue to believe the action to be without merit. Our insurance company is supporting our defense of this

action. We are working on redeveloping this property as a manufactured home community, using fill from adjacent land that we have purchased in order to comply with current codes. The adjacent parcel is also slated for manufactured home development upon receipt of appropriate permits. Redevelopment of these properties will be determined in accordance with market conditions.

In November 2013, the Company entered into an agreement with 21st Mortgage Corporation (21st Mortgage) under which the Company may refer purchasers of homes sold by us to 21st Mortgage to provide financing for their home purchases. We do not receive referral fees or other cash compensation under the agreement. If 21st Mortgage makes loans to purchasers referred by us under the agreement, and those purchasers default on their loans and 21st Mortgage repossesses the homes securing such loans, we have agreed to purchase from 21st Mortgage each such repossessed home for a price equal to 80% to 95% of the amount under each such loan, subject to certain adjustments. In addition, we have agreed to waive all site rent that would otherwise be due from 21st Mortgage so long as it owns any homes on which loans were made pursuant to the agreement. This agreement may be terminated by either party with 30 days written notice. As of March 31, 2014, there were seven transactions under this agreement in an aggregate loan amount of approximately \$300,000.

The Company has entered into definitive agreements to purchase six manufactured home communities with a total of approximately 589 developed home sites. These communities are located in Ohio and Pennsylvania. The aggregate purchase price of these communities totals approximately \$17.6 million. In conjunction with the purchase of these communities, the Company will assume mortgages totaling approximately \$8.6 million. Subject to satisfactory due diligence, we anticipate closing this transaction during the third quarter of 2014.

Since 2000, Allison Nagelberg has served as the General Counsel of both the Company and MREIC. Prior to January 1, 2014, Ms. Nagelberg was an employee of the Company pursuant to an employment agreement, dated January 1, 2012, and a portion of Ms. Nagelberg's compensation expense was reimbursed by MREIC pursuant to a cost sharing arrangement between MREIC and the Company. On January 6, 2014, Ms. Nagelberg entered into an Employment Agreement, effective January 1, 2014, with MREIC and her employment agreement with the Company was cancelled. Effective January 1, 2014, Ms. Nagelberg is employed exclusively by MREIC and none of the expense of her compensation is allocated to the Company. Mr. Craig Koster, who has been the In-House Counsel of the Company since 2012, will handle all in-house legal responsibilities for the Company.

NOTE 9 - SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest during the three months ended March 31, 2014 and 2013 was \$2,352,830 and \$1,754,064, respectively. Interest cost capitalized to Land Development was \$63,971 and \$69,976 for the three months ended March 31, 2014 and 2013, respectively.

During the three months ended March 31, 2014, the Company assumed mortgages totaling approximately \$18.1 million for the acquisition of 8 communities.

During the three months ended March 31, 2014 and 2013, the Company had Dividend Reinvestments of \$452,312 and \$341,016, respectively, which required no cash transfers.

NOTE 10 – SUBSEQUENT EVENTS

Management has evaluated subsequent events for disclosure and/or recognition in the financial statements through the date that the financial statements were issued, for which there were none.

NOTE 11 – PROFORMA FINANCIAL INFORMATION (UNAUDITED)

The following unaudited pro forma condensed financial information reflects the acquisitions during 2013 and through March 31, 2014. This information has been prepared utilizing the historical financial statements of the Company and the effect of additional Revenue and Expenses from the properties acquired during this period assuming that the acquisitions had occurred as of January 1, 2013, after giving effect to certain adjustments including: (a) Rental and Related Income; (b) community Operating Expenses; (c) Interest Expense resulting from the assumed increase in mortgages and Loans Payable related to the new acquisitions; (d) Depreciation Expense related to the new acquisitions; and (e) Net Income (Loss) Attributable to Common Shareholders which has been reduced by Preferred Dividends related to the proceeds from capital raising used for property acquisitions. The unaudited pro forma condensed financial information is not indicative of the results of operations that would have been achieved had the acquisitions reflected herein been consummated on the dates indicated or that will be achieved in the future.

	Three Months Ended	
	3/31/14	3/31/13
Rental and Related Income	\$15,466,000	\$14,786,000
Community Operating Expenses	8,522,000	7,418,000
Net Income (Loss) Attributable to		
Common Shareholders	(1,361,000)	2,045,000
Net Income (Loss) Attributable to		
Common Shareholders per Share:		
Basic	\$(0.06)	\$0.12
Diluted	\$(0.06)	\$0.12

ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

The following discussion and analysis of the consolidated financial condition and results of operations should be read in conjunction with the Consolidated Financial Statements and footnotes thereto included elsewhere herein and in our annual report on Form 10-K for the year ended December 31, 2013.

The Company is a self-administered, self-managed, REIT with headquarters in Freehold, New Jersey. The Company's primary business is the ownership and operation of manufactured home communities – leasing sites on an annual or month-to-month basis to private manufactured home owners. The Company also leases homes to residents and, through its taxable REIT subsidiary, UMH Sales and Finance, Inc. (S&F), sells and finances homes to qualified residents and prospective residents of our communities. During the quarter ended March 31, 2014, the Company acquired 8 Ohio manufactured home communities with a total of 1,018 developed homesites for a total purchase price of \$24,950,000. As of March 31, 2014, the Company owned eighty-two manufactured home communities containing approximately 14,500 developed home sites. These communities are located in New Jersey, New York, Ohio, Pennsylvania, Tennessee, Indiana and Michigan. The Company also invests in securities of other REITs.

The Company's income primarily consists of Rental and Related Income from the operation of its manufactured home communities. Income also includes sales of manufactured homes as well as sales finance operations.

Current economic indicators show the US economy to be improving and activity in our communities has recently increased. Overall occupancy has remained relatively stable at 81%. Same store occupancy has increased from 80.8% in the first quarter of 2013 to 81.8% currently. We continue to see increased demand for rental units. Recently activity includes adding approximately 300 rental units to selected communities in 2013, as well as acquiring 300 rental units during 2013 community acquisitions and we have added an additional 110 rentals in the first quarter of 2014. We intend to add more rental units throughout 2014, as demand dictates. Occupied rental units represent approximately 15% of total occupied sites at quarter end. Occupancy in rental units continues to be strong and is currently at 91% occupancy. It is our intention to continue to convert renters to new homeowners in the future.

The Company also holds a portfolio of securities of other REITs with a fair value of \$60,700,743 at March 31, 2014, which earns Dividend and Interest Income. The dividends received from our securities investments were at a weighted-average yield of approximately 6.7% during the three months ended March 31, 2014. During the three months ended March 31, 2014, the Company recognized Gains on Sales of Securities of \$508,403. At March 31, 2014, the Company had Net Unrealized Gains of \$4,438,679 in its REIT securities portfolio. The Company invests in REIT securities on margin from time to time when the Company can achieve an adequate yield spread. The REIT securities portfolio provides the Company with liquidity and additional income and serves as a proxy for real property

investments.

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The Company intends to continue to increase its real estate investments. In 2012 and 2013, we added thirty-four manufactured home communities, encompassing approximately 4,500 developed home sites, to our portfolio. On March 13, 2014, the Company acquired 8 manufactured home communities for \$24,950,000. These 8 all-age communities total 1,018 sites and are situated on approximately 270 acres. These communities are all located in Ohio. The average occupancy for these communities at closing was approximately 70%. We have also entered into a definitive agreement to purchase six manufactured home communities with a total of approximately 589 developed home sites located in Ohio and Pennsylvania for a purchase price of approximately \$17.6 million. We have been positioning ourselves for future growth and will continue to seek opportunistic investments. We currently have the potential to fill 2,800 vacancies. Housing demand in the energy-rich Marcellus and Utica shale regions where a substantial amount of our communities are located is expected to be particularly strong in the years to come and we intend to focus our acquisitions in those regions.

See PART I, Item 1 – Business in tm" STYLE="border-top:1px solid #000000">

ManTech Consolidated

\$283,695 100% \$262,431 100% \$846,466 100% \$719,300 100%

Gross profit:

Regional Logistics Support to the Warfighter

\$2,195 5% \$3,772 8% \$8,565 6% \$9,593 8%

Countermine Support

2,265 5% 0% 4,327 3% 0%

All other contracts

43,696 91% 42,399 92% 131,349 91% 117,577 92%

ManTech Consolidated

\$48,156 100% \$46,171 100% \$144,241 100% \$127,170 100%

Receivables:

Regional Logistics Support to the Warfighter

\$6,054 3% \$33,422 14%

Countermine Support

12,133 6% 0%

All other contracts

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187,550 91% 202,589 86%

ManTech Consolidated

\$205,737 100% \$236,011 100%

Disclosure items required under SFAS No. 131 including interest revenue, interest expense, depreciation and amortization, costs for stock-based compensation programs and expenditures for segment assets are not applicable as we review those items on a consolidated basis.

7. Revenues and Receivables

We deliver a broad array of information technology and technical services solutions under contracts with the U.S. government, state and local governments, and commercial customers. Revenues from the U.S. government under prime contracts and subcontracts were approximately 97.8% and 98.2% of our total revenue for the nine months ended September 30, 2006 and 2005, respectively. The components of contract receivables are as follows:

	September 30, 2006	December 31, 2005
Billed receivables	\$ 181,901	\$ 204,793
Unbilled receivables:		
Amounts billable	20,615	30,221
Revenues recorded in excess of estimated contract value or funding	2,791	4,100
Revenues recorded in excess of milestone billings on fixed price contracts	4,427	3,737
Retainage	2,064	1,935
Allowance for doubtful accounts	(6,061)	(5,110)
	\$ 205,737	\$ 239,676

Amounts billable consist principally of amounts to be billed within the next month. Revenues recorded in excess of contract value or funding are billable upon receipt of contractual amendments or other modifications. Revenues recorded in excess of milestone billings on fixed price contracts consist of amounts not expected to be billed within the next month. The retainage is billable upon completion of DCAA audit. At September 30, 2006, the amount of receivables that we expect to collect after one year is \$6.1 million.

Table of Contents**8. Commitments and Contingencies**

Payments to us on cost-reimbursable contracts with the U.S. government are provisional payments subject to adjustment upon audit by the DCAA. The majority of audits through 2002 and 2003 have been completed and resulted in no material adjustments. The audits for 2002 through 2005 are not expected to have a material effect on the results of future operations.

In the normal course of business, we are involved in certain governmental and legal proceedings, claims and disputes, and have litigation pending under several suits. We believe that the ultimate resolution of these matters will not have a material effect on our financial position or results of operations.

9. Acquisitions

Gray Hawk Systems, Inc. On May 31, 2005, we completed the acquisition of 100 percent of outstanding shares of Gray Hawk Systems, Inc. (Gray Hawk). Gray Hawk provides a broad range of intelligence-related services to the homeland security, law enforcement, Intelligence Community and the Department of Defense markets. The acquisition was consummated pursuant to an Agreement and Plan of Merger, dated May 3, 2005, which provided for the merger of a wholly owned subsidiary of ManTech with and into Gray Hawk, with Gray Hawk surviving the merger and becoming a wholly owned subsidiary of ManTech (ManTech Gray Hawk).

We believe the Gray Hawk acquisition further solidifies our position as a supplier of services in the high-end intelligence market. It expands our presence in homeland security related missions and complements our high-end offerings for the Intelligence Community and Department of Defense. Gray Hawk s capabilities round-out ManTech s skills in the end-to-end, intelligence information processing cycle, and give ManTech access to new markets in national defense agencies, which we believe will become increasingly important as the Intelligence Reform Act of 2004 continues to unfold.

The purchase price for the acquisition was \$101.8 million in cash, which included transaction costs of \$0.3 million. The purchase price included the full payment of Gray Hawk s outstanding debt, repurchase of employee stock options by Gray Hawk, transaction costs and other related transaction expenses. Pursuant to the Merger Agreement, and as security for the Gray Hawk shareholders indemnification obligations, an escrow account in an amount equal to 10% of the adjusted purchase price was established to be used in satisfying certain indemnification obligations of the shareholders of Gray Hawk. As of September 30, 2006, all but \$0.3 million has been disbursed. Of the disbursed escrow amount, \$0.1 million was paid to the Company with the balance going to Gray Hawk Shareholders. Assuming we continue to produce adequate levels of taxable income, \$72.9 million of the \$75.4 million in goodwill will be deducted for tax purposes over 15 years.

Purchase Price Allocation

The acquisition has been accounted for as a business combination. Under business combination accounting, the total purchase price was allocated to Gray Hawk s net tangible and identifiable intangible assets based on their estimated fair values as of May 31, 2005, as set forth below. The excess of the purchase price over the net tangible and identifiable intangible assets, as determined by a third party valuation firm, was recorded as goodwill. Recognition of goodwill is largely attributed to the highly skilled employees of Gray Hawk and the value paid for companies in this business. The final aspect of the purchase agreement which is not yet finalized relates to Gray Hawk shareholders indemnification obligations of \$0.3 million for uncollected receivables and tax refund payments.

(in thousands)

Cash	\$ 608
Accounts receivable	18,584
Prepaid expenses and other current assets	455
Fixed assets	799
Other assets	284
Intangible assets	15,650
Goodwill	75,389
Accounts payable	(4,345)
Payroll liabilities	(3,576)
Deferred tax liability	(1,528)
Billings in excess of revenue earned	(321)
Other liabilities	(190)

Total purchase price	\$ 101,809
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Table of Contents*Intangible Assets*

In allocating the purchase price, we considered, among other factors, our intention for future use of acquired assets, analyses of historical financial performance and estimates of future performance of Gray Hawk's contracts. Our fair value of intangible assets was based, in part, on a valuation completed by independent appraisers using an income approach and estimates and assumptions provided by management. The following table sets forth the components of intangible assets associated with the acquisition at May 31, 2005 (in thousands):

	Fair Value	Estimated Useful Life
Backlog	\$ 5,450	6 years
Customer Relationships	\$ 7,200	20 years
Intellectual Property	\$ 3,000	7 years
Total	\$ 15,650	

Customer contracts and related relationships represent the underlying relationships and agreements with Gray Hawk's existing customers. Intangible assets are being amortized using the straight-line method.

Pro Forma Financial Information

The unaudited financial information in the table below summarizes the combined results of operations of ManTech and Gray Hawk, on a pro forma basis, as though the companies had been combined as of the beginning of each of the periods presented. The pro forma financial information is presented for informational purposes only and is not indicative of the results of operations that would have been achieved if the Acquisition and borrowings under our Credit Agreement (see Note 10) had taken place at the beginning of each of the periods presented. The pro forma financial information for September 30, 2005 includes the business combination accounting effect on historical ManTech for amortization charges from acquired intangible assets, interest expense at our current level of debt, and the related tax effects.

The unaudited pro forma financial information for the nine months ended September 30, 2005 combines the historical results for ManTech and Gray Hawk for those periods. The financial information for the nine months ended September 30, 2006 is as reported in our consolidated statements of income (in thousands).

	Nine Months Ended September 30,	
	2006 (a)	2005
Revenue	\$ 846,466	\$ 750,225
Income from continuing operations-net of taxes	\$ 40,303	\$ 37,334
Net Income	\$ 36,782	\$ 33,722
Diluted earnings per share	\$ 1.09	\$ 1.02

(a) As reported**10. Debt**

We currently have a Credit and Security Agreement with Citizens Bank of Pennsylvania. The agreement initially provides for a \$125 million credit facility that can be increased to \$200 million. The maturity date of the agreement is February 25, 2009. Under the agreement, we are required to maintain specified financial covenants relating to asset coverage, fixed charge coverage, and debt coverage. The agreement also places limitations on additional borrowings, mergers, and related-party transactions, payment of dividends, and contains limitations with respect to capital expenditures. Borrowings under the agreement are collateralized by our assets and bear interest at the London Inter-Bank Offer Rate (LIBOR), or the lender's base rate, plus market-rate spreads that are determined based on a company leverage ratio calculation. As of September 30, 2006, we were in compliance with all covenants under the credit facility.

We had \$0 and \$42.4 million outstanding on our credit facility at September 30, 2006 and December 31, 2005, respectively. The maximum available borrowing under the credit facility at September 30, 2006 was \$123.4 million. As of September 30, 2006, we were contingently liable

under letters of credit totaling \$1.6 million, which reduces our availability to borrow under our credit facility.

Table of Contents**11. Discontinued Operations**

The Condensed Consolidated Financial Statements and related note disclosures reflect the ManTech MSM Security Services, Inc. (MSM) subsidiary as Long-Lived Assets to Be Disposed Of by Sale for all periods presented in accordance with SFAS No. 144 *Accounting for the Impairment or Disposal of Long-Lived Assets*. As such, MSM is classified as held for sale in the consolidated balance sheets and discontinued operations, net of applicable income taxes in the consolidated statements of income.

In 2005, we reached a final corporate determination to exit the personnel security investigation services business and discontinue operations at our MSM subsidiary. We reached the determination to sell our MSM subsidiary after we concluded that the MSM business no longer furthered our long-term strategic objectives. We intend to sell MSM as a going-concern and we are in continuing discussions with potential buyers. However, the sale has been delayed due to lower than expected results on a contract. This contract was expected to ramp up beginning in 2005 and provide considerable monthly revenues and profits for MSM. The level of anticipated growth did not occur. In July 2006, the customer procured new contracts for future work and MSM did not receive one of the new contracts. In addition, the customer determined that they would not exercise the follow on option periods on the existing contract. MSM has contracts with other customers and has recently received increased work on a continuing contract with one of these customers. We continue to market MSM and we believe there are potential buyers still interested in the acquisition of MSM and we are having continuing communications with such parties. We expect to complete a sale of MSM by the end of 2006. At December 31, 2005, we recorded a loss accrual of \$3.6 million on the valuation of these assets based on nonbinding offers received from potential buyers in early 2006. The loss accrual reflects the write-off of intangible assets including goodwill, net of taxes. The loss also reflects a valuation allowance of \$1.3 million for deferred state income tax assets related to net operating losses carried forward, which are not expected to be realized.

The following discloses the results of the discontinued operations of MSM for the three and nine months ended September 30, 2006 and 2005 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Revenue	\$ 4,118	\$ 1,570	\$ 11,095	\$ 5,173
Loss before taxes	\$ (1,807)	\$ (1,902)	\$ (5,825)	\$ (5,759)
Net Loss	\$ (1,092)	\$ (1,167)	\$ (3,521)	\$ (3,481)

The following is a summary of the assets and liabilities held for sale related to MSM at September 30, 2006 and December 31, 2005 (in thousands):

	September 30, 2006	December 31, 2005
Receivables, net	\$ 3,524	\$ 1,540
Prepaid expenses and other	69	67
Property and equipment	802	710
Other assets	1,430	2,029
Total Assets	\$ 5,825	\$ 4,346
Accounts payable and accrued expenses	\$ 586	\$ 963
Accrued salaries and related expenses	464	444
Billings in excess of revenue earned	2,711	3,410
Other liabilities	55	58
Total Liabilities	\$ 3,816	\$ 4,875

Table of Contents**12. Gain on Disposal of an Operation**

On February 11, 2005, we sold our Mantech Environmental Technology, Inc (METI) subsidiary to another company, Alion Science and Technology Corporation. METI performs professional services including research and development in the fields of environmental and life sciences for the Environmental Protection Agency, the National Cancer Institute, the U.S. Air Force, and other federal government agencies. The financial terms of the arrangement included an all cash payment of \$7 million, which resulted in a pre-tax gain of approximately \$3.7 million, net of selling costs, in the first quarter of 2005. After the sale, we continue to provide professional services in the environmental area for various federal government agencies.

The following discloses the results of METI for the three and nine months ended September 30, 2005 (METI's results for 2005 are through February 11th) (in thousands):

	Nine Months Ended September 30, 2005
Revenue	\$ 1,379
Income before taxes	\$ 55
Net Income	\$ 34

13. Financial Guarantees

Effective July 11, 2003, our lenders issued two letters of credit to Fianzas Guardiania Inbursa, S.A. (FGI) on behalf of GSE Systems, Inc (GSE). When the letters of credit were issued, we held an investment in GSE that was accounted for under the equity method. On October 21, 2003, we sold all of our equity interests in GSE to GP Strategies Corporation (GP Strategies) in exchange for a note with a principle amount of \$5.3 million. The note from GP Strategies bears interest at 5.0% per annum and is payable quarterly in arrears. Each year during the term of the note, we have an option to convert up to 20% of the original principal amount of the note into common stock of GP Strategies, but only in the event that GP Strategies' common stock is trading at \$10 per share or more. As of September 30, 2006, we have not converted any of the principal to GP Strategies' common stock.

During 2006, George J. Pedersen, our Chairman and Chief Executive Officer, beneficially owned shares and options of GSE stock representing less than 5% of GSE. In 2006, Mr. Pedersen served on GSE's board of directors and compensation committee.

The first letter of credit in support of an advance payment bond of approximately \$1.8 million, issued by FGI to a customer of GSE's power business was cancelled in March of 2005. The second letter of credit, which was in support of a performance bond of approximately \$1.3 million issued by FGI to the same customer, was cancelled in August 2006. In exchange for issuing the letters of credit, we received 100,000 warrants to purchase GSE's common stock at the market price of GSE's common stock as of the close of business on July 8, 2003, and received a 7% annual fee, payable on a quarterly basis, calculated on the total amount of the then-existing value of the letters of credit.

14. Subsequent Events

On October 5, 2006, we completed the acquisition of all outstanding shares of GRS Solutions, Inc. (GRS) for \$18.0 million in cash, subject to adjustment upon finalizing the closing balance sheet and certain shareholder indemnification obligations. The source of funds for the acquisition was our available cash.

GRS is a privately held company headquartered in Falls Church, VA providing specialized technical, operational and analytical services to the Intelligence Community. The acquisition improves our strategic position within the intelligence community and strengthens our capabilities in supporting counterterrorism/counterintelligence missions around the world. For its fiscal year ended September 30, 2006, GRS had revenues of approximately \$10.0 million.

The initial purchase price was \$18.0 million. As security for the GRS shareholders' indemnification obligations, an escrow account in an amount of \$1.8 million was established to be used in satisfying certain indemnification obligations of the shareholders of GRS. In addition, contingent consideration of \$2.0 million based on a defined performance objective was met subsequent to the initial purchase. The purchase price and contingent consideration will be allocated to the underlying assets and liabilities based on their estimated fair values.

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On October 31, 2006, we completed the sale of assets related to our NetWitness® business to the NetWitness Acquisition Corp. NetWitness® is a network forensics product used to analyze and model complex network traffic. The business consists of the software product, trademark, contracts, and a support staff of eleven people. The financial terms of the arrangement include a cash payment of \$2.0 million and an equity stake of less than 5% in the NetWitness Acquisition Corp.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations****Introduction and Overview**

We are a leading provider of innovative technologies and solutions for mission-critical national security programs for the Intelligence Community; the Departments of Defense, State, Homeland Security and Justice; the Space Community; and other U.S. federal government agencies. Our expertise includes systems engineering, systems integration, software services, enterprise architecture, information assurance and security architecture, intelligence operations and analysis support, network and critical infrastructure protection, information operations and computer forensics, information technology, communications integration and engineering support. With nearly 5,800 highly qualified employees, we operate in the United States and over 40 countries worldwide.

We derive revenue primarily from contracts with U.S. government agencies that are focused on national security and as a result, funding for our programs is generally linked to trends in U.S. government spending in the areas of defense, intelligence and homeland security. Leading up to and following the terrorist events of September 11, 2001, the U.S. government substantially increased its overall defense, intelligence and homeland security budgets.

We recommend that you read this discussion and analysis in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations included in our annual report on Form 10-K for the fiscal year ended December 31, 2005, previously filed with the SEC.

Three Months Ended September 30, 2006 Compared to the Three Months Ended September 30, 2005

	Consolidated Statements of Operations					
	Three Months Ended September 30,		2006		Period to Period Change	
	2006	2005	2006	2005	2005 to 2006	
	Dollars		Percentages	Dollars	Percent	
	(dollar amounts in thousands)					
REVENUE	\$ 283,695	\$ 262,431	100.0%	100.0%	\$ 21,264	08.1%
COST OF SERVICES	235,539	216,260	83.0%	82.4%	19,279	08.9%
GROSS PROFIT	48,156	46,171	17.0%	17.6%	1,985	04.3%
COSTS AND EXPENSES:						
General & administration	22,951	22,327	08.1%	08.5%	624	02.8%
Depreciation & amortization	2,191	2,008	00.8%	00.8%	183	09.1%
Total costs and expenses:	25,142	24,335	08.9%	09.3%	807	03.3%
INCOME FROM CONTINUING OPERATIONS:	23,014	21,836	08.1%	08.3%	1,178	05.4%
Interest (expense), net	(291)	(1,120)	00.1%	00.4%	829	-74.0%
Equity in earnings of affiliates		157	00.0%	00.1%	(157)	-100.0%
Other income (expense), net	21	(52)	00.0%	00.0%	73	140.4%
INCOME BEFORE PROVISION FOR INCOME TAXES AND MINORITY INTEREST	22,744	20,821	08.0%	07.9%	1,923	09.2%
Provision for income taxes	(8,962)	(7,833)	03.2%	03.0%	(1,129)	14.4%
Minority interest		(3)	00.0%	00.0%	3	-100.0%
INCOME FROM CONTINUING OPERATIONS - net of taxes	13,782	12,985	04.9%	04.9%	797	06.1%
(Loss) income from discontinued operations-net of taxes	(1,092)	(1,298)	00.4%	00.5%	206	-15.9%
NET INCOME	\$ 12,690	\$ 11,687	04.5%	04.5%	\$ 1,003	08.6%

Table of Contents*Revenues*

Revenues increased 8.1% to \$283.7 million for the three months ended September 30, 2006, compared to \$262.4 million for the same period in 2005. This increase is partially attributable to forward deployment support in Iraq and Afghanistan and increased work in the Intelligence Community. The loss of a Department of State contract as of June 30, 2006 slowed our growth in this quarter by approximately \$7.3 million as compared to the same period in 2005.

Cost of services

Cost of services increased 8.9% to \$235.5 million for the three months ended September 30, 2006, compared to \$216.3 million for the same period in 2005. As a percentage of revenues, cost of services increased 0.6%, to 83.0% for the three months ended September 30, 2006 compared to 82.4% for the same period in 2005. The increase in costs of services is largely attributable to increased purchases of subcontractors and equipment and materials used in the performance of our contracts. Direct labor costs, which includes applicable fringe benefit and overhead, was down slightly quarter over quarter. This decrease was primarily due to a reduction in our employee benefit cost. As a percentage of revenues, direct labor costs decreased 3.8% to 43.8% for the three months ended September 30, 2006 compared to 47.6% for the same period in 2005 due primarily to the increase in cost and related revenue from subcontractors and equipment and materials. For the three months ended September 30, 2006, other direct costs increased by 21.7% over the same quarter in 2005, from \$91.4 million to \$111.2 million, which reflects the increase in purchases of subcontractors and equipment and materials, as noted above. As a percentage of revenues, other direct costs increased from 34.8% for the three months ended September 30, 2005 to 39.2% for the same period in 2006.

Gross profit

Gross profit increased 4.3% to \$48.2 million for the three months ended September 30, 2006, compared to \$46.2 million for the same period in 2005. Gross profit margin was 17.0% for the three months ended September 30, 2006, compared to 17.6% for the same period in 2005. The decrease in gross profit margin is primarily due to a less profitable mix of reimbursable items including subcontractors and material purchases which increased cost of services as a percentage of revenue.

General and administrative

General and administrative expenses increased 2.8% to \$23.0 million for the three months ended September 30, 2006, compared to \$22.3 million for the same period in 2005. As a percentage of revenues, general and administrative expenses decreased to 8.1% from 8.5% for the three months ended September 30, 2006 and 2005, respectively. The increase in expense during the three months ended September 30, 2006 resulted primarily from the adoption of SFAS No. 123R. This increase was partially offset by a decrease in bid and proposal spending. Bid and proposal spending was higher in 2005 due to several key contracts being recompleted. Under SFAS No. 123R, share-based payments not fully vested as of January 1, 2006 and those granted after January 1, 2006 are measured at estimated fair value and included as compensation expense over the periods service is provided. For the three months ended September 30, 2006, we recognized \$1.3 million in compensation costs in accordance with SFAS No. 123R. Excluding the impact of SFAS No. 123R, general and administrative expense as a percentage of revenue was 7.6% for the three months ended September 30, 2006. The lower percentage reflects management's efforts to improve operating efficiency even though revenues increased by 8.1%.

Depreciation and amortization

Depreciation and amortization expense increased 9.1% to \$2.2 million for the three months ended September 30, 2006, compared to \$2.0 million for the same period in 2005. The increase was primarily due to the additional amortization of intangibles and an increase in leasehold improvements related to new office space and general improvements.

Interest expense, net

Interest expense, net decreased 74.0% to \$0.3 million for the three months ended September 30, 2006, compared with \$1.1 million for the same period in 2005. The decrease in interest expense, net is a result of paying off our line of credit and higher interest income due to increased cash on hand for the period ended September 30, 2006. The average levels of indebtedness were approximately \$29.6 million and \$81.0 million, in the three months ended September 30, 2006 and 2005, respectively. The higher average level of indebtedness in 2005 was due to our acquisition of Gray Hawk in May 2005. As we intend to use our credit facility to finance our acquisition strategy, interest expense levels could increase with the acquisition of other operations.

Net income

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Net income increased 8.6% to \$12.7 million for the three months ended September 30, 2006, compared to \$11.7 million for the same period in 2005. The increase is a result of higher revenue, increased income from continuing operations and reduced interest expense, net. Our losses in discontinued operations decreased due to higher revenue from increased case completion at our MSM subsidiary. Our effective tax rate for the three months ended September 30, 2006 and 2005 was 39.4% and 37.6%, respectively.

Table of Contents*Nine Months Ended September 30, 2006 Compared to the Nine Months Ended September 30, 2005*

	Consolidated Statements of Operations					
	Nine Months Ended September 30,				Period to Period Change	
	2006	2005	2006	2005	2005 to 2006	
	Dollars		Percentages		Dollars	Percent
	(dollar amounts in thousands)					
REVENUE	\$ 846,466	\$ 719,300	100.0%	100.0%	\$ 127,166	17.7%
COST OF SERVICES	702,225	592,130	83.0%	82.3%	110,095	18.6%
GROSS PROFIT	144,241	127,170	17.0%	17.7%	17,071	13.4%
COSTS AND EXPENSES:						
General & Administration	69,731	62,510	08.2%	08.7%	7,221	11.6%
Depreciation & amortization	6,327	5,147	00.7%	00.7%	1,180	22.9%
Total costs and expenses:	76,058	67,657	09.0%	09.4%	8,401	12.4%
INCOME FROM CONTINUING OPERATIONS:	68,183	59,513	08.1%	08.3%	8,670	14.6%
Interest (expense), net	(1,684)	(1,956)	00.2%	00.3%	272	-13.9%
Equity in earnings of affiliates		435	00.0%	00.1%	(435)	-100.0%
Gain on disposal of an operation		3,698	00.0%	00.5%	(3,698)	-100.0%
Other income (expense), net	8	(228)	00.0%	00.0%	236	103.5%
INCOME BEFORE PROVISION FOR INCOME TAXES AND MINORITY INTEREST	66,507	61,462	07.9%	08.5%	5,045	08.2%
Provision for income taxes	(26,204)	(24,085)	03.1%	03.3%	(2,119)	08.8%
Minority interest		(9)	00.0%	00.0%	9	-100.0%
INCOME FROM CONTINUING OPERATIONS - net of taxes	40,303	37,368	04.8%	05.2%	2,935	07.9%
(Loss) income from discontinued operations-net of taxes	(3,521)	(3,612)	00.4%	00.5%	91	-02.5%
NET INCOME	\$ 36,782	\$ 33,756	04.3%	04.7%	\$ 3,026	09.0%

Revenues

Revenues increased 17.7% to \$846.5 million for the nine months ended September 30, 2006, compared to \$719.3 million for the same period in 2005. This increase is partially attributable to forward deployment support in Iraq and Afghanistan and increased work in the Intelligence Community. Also contributing to the increase was three full quarters of revenues from our acquisition of Gray Hawk Systems, Inc. (Gray Hawk) on May 31, 2005. Gray Hawk accounted for \$37.6 million of our increase in revenue period over period.

Cost of services

Cost of services increased 18.6% to \$702.2 million for the nine months ended September 30, 2006, compared to \$592.1 million for the same period in 2005. As a percentage of revenues, cost of services increased 0.7%, to 83.0% for the nine months ended September 30, 2006 compared to 82.3% for the same period in 2005. This increase was due to larger purchases of equipment and materials directly for contracts and the use of subcontractors in support of our contracts. Direct labor costs, which include applicable fringe benefits and overhead, increased by 11.3% primarily due to the addition of Gray Hawk and the growth of our business. As a percentage of revenues, direct labor costs decreased 2.6% to 45.6% for the nine months ended September 30, 2006 compared to 48.2% for the same period in 2005. For the nine months ended September 30, 2006, other direct costs increased by 28.9% over the same period in 2005, from \$245.5 million to \$316.5 million, which reflects the increase in purchases of subcontractors and equipment and materials, as noted above. As a percentage of revenues, other direct costs increased from 34.1% for the nine months ended September 30, 2005 to 37.4% for the same period in 2006.

Gross profit

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Gross profit increased 13.4% to \$144.2 million for the nine months ended September 30, 2006, compared to \$127.2 million for the same period in 2005. Gross profit margin was 17.0% for the nine months ended September 30, 2006, compared to 17.7% for the same period in 2005. The decrease in gross profit margin is primarily due to a less profitable mix of reimbursable items including subcontractors and material purchases which increased cost of services as a percentage of revenue.

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General and administrative

General and administrative expenses increased 11.6% to \$69.7 million for the nine months ended September 30, 2006, compared to \$62.5 million for the same period in 2005. As a percentage of revenues, general and administrative expenses decreased to 8.2% from 8.7% for the nine months ended September 30, 2006 and 2005, respectively. The increase in expense during the nine months resulted primarily from the adoption of SFAS No. 123R and the addition of Gray Hawk in May 2005. This increase was partially offset by a decrease in bid and proposal spending. Under SFAS No. 123R, share-based payments not fully vested as of January 1, 2006 and those granted in the nine months ended September 30, 2006 are measured at estimated fair value and included as compensation expense over the periods service is provided. For the nine months ended September 30, 2006, we recognized \$4.0 million in compensation costs in accordance with SFAS No. 123R. Excluding the impact of SFAS No. 123R, general and administrative expense as a percentage of revenue was 7.8% for the nine months ended September 30, 2006. The lower percentage reflects management's efforts to improve operating efficiency even though revenues increased by 17.7%.

Depreciation and amortization

Depreciation and amortization expense increased 22.9% to \$6.3 million for the nine months ended September 30, 2006, compared to \$5.1 million for the same period in 2005. The increase was primarily due to the additional amortization of intangibles from the Gray Hawk acquisition and an increase in leasehold improvements related to new office space and general improvements.

Interest expense, net

Interest expense, net decreased 13.9% to \$1.7 million for the nine months ended September 30, 2006, compared with \$2.0 million for the same period in 2005. The decrease in interest expense is a result of decreased borrowing under our credit facility in 2006. The higher level of indebtedness in 2005 was due to our acquisition of Gray Hawk Systems in May 2005. As we intend to use our credit facility to finance our acquisition strategy, interest expense levels could increase with the acquisition of other operations.

Gain on disposal of an operation

On February 11, 2005, we sold our Mantech Environmental Technology, Inc (METI) subsidiary to Alion Science and Technology Corporation. The sale generated a pre-tax gain of \$3.7 million in 2005. For additional information see [Gain on Disposal of an Operation](#), below.

Net income

Net income increased 9.0% to \$36.8 million for the nine months ended September 30, 2006, compared to \$33.8 million for the same period in 2005. The increase is a result of higher revenue and increased income from continuing operations. In addition, we recorded a \$1.8 million after-tax gain recorded in 2005 on the sale of METI. Our effective tax rate for the nine months ended September 30, 2006 and 2005 was 39.4% and 39.2%, respectively.

Backlog

At September 30, 2006 and December 31, 2005, our backlog was \$2.7 billion and \$2.3 billion, respectively, of which \$504 million and \$467 million, respectively, was funded backlog. At September 30, 2005, our backlog was \$1.9 billion, of which \$439 million was funded backlog. Backlog and funded backlog represent estimates that we calculate on a consistent basis. Additional information on how we determine backlog is included in our annual report on Form 10-K for the fiscal year ended December 31, 2005, previously filed with the SEC. The increase in backlog was primarily attributable to the award for work currently under the Regional Support of the War fighter contract listed in footnote 6 of the financial statements.

Effects of Inflation

We generally have been able to price our contracts in a manner to accommodate the rates of inflation experienced in recent years. Under our time and materials contracts, labor rates are usually adjusted annually by predetermined escalation factors. Our cost reimbursable contracts automatically adjust for changes in cost. Under our fixed-price contracts, we include a predetermined escalation factor, but generally, we have not been adversely affected by inflation.

Liquidity and Capital Resources

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Our primary liquidity needs are the financing of working capital, capital expenditures and acquisitions. Our primary source of liquidity is cash provided by operations and our \$125.0 million revolving credit facility. At September 30, 2006, we did not have an outstanding balance under our credit facility. At September 30, 2006, we were contingently liable under letters of credit totaling \$1.6 million, which reduces our ability to borrow under our credit facility. The maximum available borrowing under our

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credit facility at September 30, 2006 was \$123.4 million. Generally, cash provided by operating activities is adequate to fund our operations. Due to fluctuations in our cash flows and the growth in our operations, it is necessary from time to time to increase borrowings under our credit facility to meet cash demands. In the future, we may borrow greater amounts in order to finance acquisitions or new contract start ups.

Net cash flows from operating activities

(in thousands)	Nine months ended September 30,	
	2006	2005
Cash provided by operating activities from continuing operations:	\$ 83,026	\$ 23,872
Cash (used) provided by discontinued operations:	(5,881)	14,137
Cash provided by operating activities:	\$ 77,145	\$ 38,009

Cash provided by operating activities for the nine months ended September 30, 2006 was \$77.1 million, compared to \$38.0 million provided by operating activities for the nine months ended September 30, 2005. The increase in cash provided in 2006 was primarily due to the significant collections of receivables. The significant collections were the results of a very focused effort by management. In addition, net cash flows from operating activities was impacted by the adoption of SFAS No. 123R, which required the reclassification of excess tax benefits from the exercise of stock options from operating cash flows to financing cash flows. For the nine months ended September 30, 2005, discontinued operations provided \$14.1 million of cash inflow versus a net use of cash of \$5.9 million for the nine months ended September 30, 2006. Net cash inflow from discontinued operations in 2005 was primarily due to collections on our Defense Security Services contract of \$16.4 million.

Net cash flows from investing activities

(in thousands)	Nine months ended September 30,	
	2006	2005
Cash used in investing activities from continuing operations:	\$ (5,708)	\$ (106,453)
Cash used in investing activities from discontinued operations:	(125)	(355)
Cash used in investing activities:	\$ (5,833)	\$ (106,808)

Cash used in investing activities was \$5.8 million for the nine months ended September 30, 2006, compared to a cash outflow of \$106.8 million for the same period in 2005. The cash outflow in 2006 is primarily the result of investments in property, plant, and equipment and internal-use software. For the same period in 2005, the cash outflow is primarily due to the acquisition of Gray Hawk in May of 2005 for \$101.2 million, net of cash acquired and final earnout payments related to our acquisition of IDS in 2003.

Subsequent to September 30, 2006, we acquired GRS Solutions, Inc for an initial purchase price of \$18.0 million in cash on October 5, 2006. In addition, on October 31, 2006 we sold assets related to our NetWitness® business for \$2.0 million in cash. For additional information, see Note 14 Subsequent Events in our condensed consolidated financial statements.

Net cash flows from financing activities

(in thousands)	Nine months ended September 30,	
	2006	2005

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Cash (used) provided by financing activities:	\$	(29,637)	\$	59,141
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Cash used in financing activities was \$29.6 million for the nine months ended September 30, 2006, compared to cash provided by financing activities of \$59.1 million for the nine months ended September 30, 2005. The net cash used in the first nine months of 2006 resulted primarily from paying down our line of credit with cash provided from operations, \$42.4 million, offset by cash inflows from the exercise of stock options of \$10.3 million and the impact of SFAS No. 123R. SFAS 123R requires that excess tax benefits be shown as a cash inflow from financing activities. The net cash provided in the nine months ended September 30, 2005 resulted from proceeds from the exercise of stock options of \$9.2 million and use of our line of credit of \$50.0 million to finance our acquisition of Gray Hawk.

Table of Contents*Credit Agreement*

We currently have a Credit and Security Agreement with Citizens Bank of Pennsylvania. The agreement initially provides for a \$125.0 million credit facility that can be increased to \$200.0 million. The maturity date of the agreement is February 25, 2009. Under the agreement, we are required to maintain specified financial covenants relating to asset coverage, fixed charge coverage, and debt coverage. The agreement also places limitations on additional borrowings, mergers, and related-party transactions, payment of dividends, and contains limitations with respect to capital expenditures. Borrowings under the agreement are collateralized by our assets and bear interest at the London Interbank Offered Rate (LIBOR), or the lender's base rate, plus market-rate spreads that are determined based on a company leverage ratio calculation. As of September 30, 2006, we were in compliance with all material covenants under the credit facility.

We believe the capital resources available to us under our credit facility and cash from our operations are adequate to fund our ongoing operations and to support the internal growth we expect to achieve for at least the next twelve months. We anticipate financing our external growth from acquisitions and our longer-term internal growth through one or more of the following sources: cash from operations; additional borrowing; issuance of equity; use of the credit facility; or a refinancing of our credit facility.

Off-Balance Sheet Arrangements

Effective June 20, 2003, our lenders issued two letters of credit to Fianzas Guardiania Inbursa, S.A. (FGI) on behalf of GSE Systems, Inc. (GSE). As discussed in note 13 to our consolidated financial statements, prior to the sale of these investments on October 21, 2003, we held common and preferred stock in GSE and accounted for this investment using the equity method.

The first letter of credit, which was cancelled in March 2005, was in support of an advance payment bond of approximately \$1.8 million, issued by FGI to a customer of GSE's power business and had a term of 30 months. The second letter of credit, which was in support of a performance bond of approximately \$1.3 million issued by FGI to the same customer, was cancelled in August 2006. In exchange for issuing the letters of credit, we received 100,000 warrants to purchase GSE's common stock at the market price of GSE's common stock as of the close of business on July 8, 2003, and received a 7% annual fee, payable on a quarterly basis, calculated on the total amount of the then-existing value of the letters of credit.

During 2006, George J. Pedersen, our Chairman of the Board and Chief Executive Officer, beneficially owned shares and options of GSE stock representing less than 5% of GSE. In 2006, Mr. Pedersen served on GSE's board of directors and compensation committee.

Gain on Disposal of an Operation

On February 11, 2005, we sold our METI subsidiary to another company, Alion Science and Technology Corporation. METI performs research and development in the fields of environmental and life sciences for the Environmental Protection Agency, the National Cancer Institute, the U.S. Air Force, and other federal government agencies. The financial terms of the arrangement included an all cash payment of \$7 million, which resulted in a pre-tax gain of approximately \$3.7 million net of selling cost in the nine months ended September 30, 2005. Although we have sold METI, we continue to provide professional services in the environmental area for various federal government agencies.

Discontinued Operations

The Condensed Consolidated Financial Statements and related note disclosures reflect the ManTech MSM Security Services, Inc. (MSM) subsidiary as *Long-Lived Assets to Be Disposed Of by Sale* for all periods presented in accordance with SFAS No. 144 *Accounting for the Impairment or Disposal of Long-Lived Assets*. As such, MSM is classified as held for sale in the consolidated balance sheets and discontinued operations, net of applicable income taxes in the consolidated statements of income.

In 2005, we reached a final corporate determination to exit the personnel security investigation services business and discontinue operations at our MSM subsidiary. We reached the determination to sell our MSM subsidiary after we concluded that the MSM business no longer furthered our long-term strategic objectives. We intend to sell MSM as a going-concern and we are in continuing discussions with potential buyers. However, the sale has been delayed due to lower than expected results on a contract. This contract was expected to ramp up beginning in 2005 and provide considerable monthly revenues and profits for MSM. The level of anticipated growth did not occur. In July 2006, the customer procured new contracts for future work and MSM did not receive one of the new contracts. In addition, the customer determined that they would not exercise the follow on option periods on the existing contract. MSM has contracts with other customers and has recently received considerable increased work on a continuing contract with one of these customers. We believe this trend of additional customer demand will continue into the near future. We continue to market MSM and we believe there are potential buyers still interested in the acquisition of MSM and we are having continuing communications with such parties. We expect to complete a sale of MSM by the end of 2006. At December 31,

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2005, we recorded a loss accrual of \$3.6 million on the valuation of these assets based on nonbinding offers received from potential buyers in early 2006. The loss accrual reflects the write-off of intangible assets including goodwill, net of taxes. The loss also reflects a valuation allowance of \$1.3 million for deferred state income tax assets related to net operating losses carried forward, which are not expected to be realized.

Table of Contents**Critical Accounting Estimates and Policies**

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and potentially result in materially different results under different assumptions and conditions. Application of these policies is particularly important to the portrayal of our financial condition and results of operations. The discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these consolidated financial statements requires management to make estimates and judgments that affect the reported amount of assets, liabilities, revenues and expenses. Actual results may differ from these estimates under different assumptions or conditions. Our significant accounting policies, including the critical policies listed below, are described in the notes to the condensed consolidated financial statements included in this report.

Revenue Recognition and Cost Estimation

We recognize revenue when persuasive evidence of an arrangement exists, services have been rendered, the contract price is fixed or determinable, and collectibility is reasonably assured. We have a standard internal process that we use to determine whether all required criteria for revenue recognition have been met.

Our revenues consist primarily of services provided by our employees, and to a lesser extent, the pass through of costs for materials and subcontract efforts under contracts with our customers. Cost of services consists primarily of compensation expenses for program personnel, the fringe benefits associated with this compensation, and other direct expenses incurred to complete programs, including cost of materials and subcontract efforts.

We derive the majority of our revenue from cost-plus-fixed-fee, cost-plus-award-fee, firm-fixed-price, or time-and-materials contracts. Revenues for cost-reimbursement contracts are recorded as reimbursable costs are incurred, including an estimated share of the applicable contractual fees earned. For performance-based fees under cost reimbursable contracts, that are subject to the provisions of Statement of Position 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts* (SOP 81-1), we recognize the relevant portion of the expected fee to be awarded by the client at the time such fee can be reasonably estimated, based on factors such as our prior award experience and communications with the client regarding performance. For cost reimbursable contracts with performance-based fee incentives that are subject to the provisions of U.S. Securities and Exchange Commission Staff Accounting Bulletin No. 104, *Revenue Recognition (SAB104)*, we recognize the relevant portion of the fee upon customer approval. For time-and-material contracts, revenue is recognized to the extent of billable rates times hours delivered plus material and other reimbursable costs incurred. For long-term fixed-price production contracts, revenue is recognized at a rate per unit as the units are delivered, or by other methods to measure services provided. Revenue from other long-term fixed-price contracts is recognized ratably over the contract period or by other appropriate methods to measure services provided. Contract costs are expensed as incurred except for certain limited long-term contracts noted below. For long-term contracts which are specifically described in the scope section of American Institute of Certified Public Accountants (AICPA) Statement of Position (SOP) No. 81-1, *Accounting for Performance of Construction Type and Certain Production-Type Contracts*, or other appropriate accounting literature we apply the percentage of completion method. Under the percentage of completion method, income is recognized at a consistent profit margin over the period of performance based on estimated profit margins at completion of the contract. This method of accounting requires estimating the total revenues and total contract cost at completion of the contract. During the performance of long-term contracts, these estimates are periodically reviewed and revisions are made as required. The impact on revenue and contract profit as a result of these revisions is included in the periods in which the revisions are made. This method can result in the deferral of costs or the deferral of profit on these contracts. Because we assume the risk of performing a fixed-price contract at a set price, the failure to accurately estimate ultimate costs or to control costs during performance of the work could result, and in some instances has resulted, in reduced profits or losses for such contracts. Estimated losses on contracts at completion are recognized when identified. In certain circumstances, revenues are recognized when contract amendments have not been finalized.

Goodwill

Goodwill represents the excess of cost over the fair value of net tangible and identifiable intangible assets of acquired companies. Effective January 1, 2002, we adopted SFAS No. 142, and no longer amortize goodwill; rather, we review goodwill at least annually for impairment. We have elected to perform this review annually during second quarter of each calendar year and have determined no adjustments are necessary at this time. For acquisitions completed prior to the adoption of SFAS No. 141 and SFAS No. 142 on January 1, 2002, goodwill was amortized on a straight-line basis over periods ranging from two to twenty years.

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Other Matters

Our significant accounting policies, including the critical policies listed above, are described in the notes to the consolidated financial statements for the year ended December 31, 2005, included in our Annual Report on Form 10-K filed with the SEC on March 10, 2006.

Recent Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123 (revised 2004), *Share-Based Payment*, which requires the compensation costs related to share-based payment transactions be recognized in financial statements. With limited exceptions, the amount of compensation will be measured based on the grant-date fair value of the equity instruments issued. Compensation cost will be recognized over the vesting period during which an employee provides service in exchange for the award. SFAS No. 123(R) was effective January 1, 2006 for the company. We have adopted the modified prospective method for reporting utilizing the Black-Scholes model for valuing our stock-based compensation on date of grant.

Information about the fair value of stock options under the Black-Scholes model and its pro forma impact on the Company's net earnings and earnings per share for the historical periods is illustrated in Note 4 of our financial statements under Stock-based Compensation disclosure.

In July 2006, the FASB issued Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes* an interpretation of FASB Statement No. 109, which clarifies the accounting for uncertainty in tax positions. FIN 48 seeks to reduce the diversity in accounting practices used in regards to uncertain tax positions by prescribing a recognition threshold and measurement criteria for benefits related to income taxes. The provisions of FIN 48 are effective for all reporting periods beginning after December 15, 2006. At this time, we are assessing the impact of the adoption of FIN 48 will have on our statement of financial position and statement of operations.

In September 2006, the FASB issued Statement No. 157 (SFAS No. 157), *Fair Value Measurements* , which addresses how companies should measure fair value when they are required to use a fair value measure for recognition or disclosure purposes under generally accepted accounting principles. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. At this time, we are assessing the impact of the adoption of SFAS No. 157 will have on our statement of financial position and statement of operations.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements that involve substantial risks and uncertainties, many of which are outside of our control. ManTech believes these statements to be within the definition of the Private Securities Litigation Reform Act of 1995. You can identify these statements by forward-looking words such as *may, will, expect, intend, anticipate, believe, estimate,* similar words. You should read statements that contain these words carefully because they discuss our future expectations, make projections of our future results of operations or financial condition or state other forward-looking information. continue

Although forward-looking statements in this Quarterly Report reflect the good faith judgment of management, such statements can only be based on facts and factors currently known by us. Consequently, forward-looking statements are inherently subject to risks and uncertainties, and actual results and outcomes may differ materially from the results and outcomes discussed in or anticipated by the forward-looking statements. We believe that it is important to communicate our future expectations to our investors. However, there may be events in the future that we are not able to predict accurately or control. Factors that could cause actual results to differ materially from the results we anticipate include, but are not limited to, the following:

adverse changes in U.S. government spending priorities;

failure to retain existing U.S. government contracts, win new contracts or win recompetes;

uncertainties specifically related to discontinued operations, including our ability to sell or dispose of our MSM operations on terms that are favorable to us, or at all;

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adverse results of U.S. government audits of our government contracts;

adverse effect of contract consolidations;

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adverse changes in our mix of contract types;

additional risks and costs associated with complying with new laws and regulations relating to corporate governance issues;

risk of contract performance or termination;

failure to obtain option awards, task orders or funding under contracts;

failure to successfully integrate recently acquired companies or businesses into our operations or to realize any accretive or synergistic effects from such acquisitions;

failure to identify, execute or effectively integrate future acquisitions;

risks associated with complex U.S. government procurement laws and regulations; and

competition.

We urge you not to place undue reliance on these forward-looking statements, which speak only as of the date of this Quarterly Report. These and other risk factors are more fully described and discussed in our annual report on Form 10-K for the fiscal year ended December 31, 2005, previously filed with the SEC, those referenced in Item 1A of Part II below, and from time to time, in our other filings with the SEC. We undertake no obligation to revise or update any forward-looking statements in order to reflect any event or circumstance that may arise after the date of this Quarterly Report. We also suggest that you carefully review and consider the various disclosures made in this Quarterly Report that attempt to advise interested parties of the risks and factors that may affect our business, financial condition, results of operations and prospects.

Item 3. Quantitative and Qualitative Disclosure about Market Risk

Our exposure to market risk relates to changes in interest rates for borrowings under our senior term loan and revolving credit facility. These borrowings bear interest at variable rates. As of September 30, 2006, we had no borrowings outstanding under our revolving credit facility. A hypothetical 10% increase in interest rates would have increased our interest expense for the three months ended September 30, 2006 by less than \$0.2 million.

We do not use derivative financial instruments for speculative or trading purposes. We invest our excess cash in short-term, investment grade, interest-bearing securities. Our investments are made in accordance with an investment policy approved by the board of directors. Under this policy, no investment securities can have maturities exceeding one year, and the average maturity of the portfolio cannot exceed 90 days.

Item 4. Controls and Procedures

As of September 30, 2006, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial officer, respectively), management evaluated the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15 of the Exchange Act. Based upon this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective, as of the end of the period covered by this report, such that the information relating to us that is required to be disclosed in our reports filed with the SEC (i) is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and (ii) is accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

There were no changes in our internal control over financial reporting during the Company's last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II OTHER INFORMATION

Item 1. Legal Proceedings

We are subject to certain legal proceedings, government audits, investigations, claims and disputes that arise in the ordinary course of our business. Like most large government defense contractors, our contract costs are audited and reviewed on a continual basis by an in-house staff of auditors from the Defense Contract Auditing Agency. In addition to these routine audits, we are subject from time to time to audits and investigations by other agencies of the federal government. These audits and investigations are conducted to determine if our performance and administration of our government contracts are compliant with contractual requirements and applicable federal statutes and regulations. An audit or investigation may result in a finding that our performance, systems and administration is compliant or, alternatively, may result in the government initiating proceedings against us or our employees, including administrative proceedings seeking repayment of monies, suspension and/or debarment from doing business with the federal government or a particular agency, or civil or criminal proceedings seeking penalties and/or fines. Audits and investigations conducted by the federal government frequently span several years.

Although we cannot predict the outcome of these and other legal proceedings, investigations, claims and disputes, based on the information now available to us, we do not believe the ultimate resolution of these matters, either individually or in the aggregate, will have a material adverse effect on our business, prospects, financial condition or operating results.

Item 1A. Risk Factors

Other than as set forth below, there have been no material changes from the risk factors disclosed in the Risk Factors section of the Company's Annual Report on Form 10-K for the year ended December 31, 2005. The risk factor stated below was disclosed on our Form 10-K and has been updated to reflect management's current expectation regarding the timing of the disposition of MSM.

We may be exposed to liabilities or losses from operations that we have or will discontinue or otherwise sell, including our MSM subsidiary.

In 2005, we reached a final corporate determination to exit the personnel security investigation (PSI) services business and discontinue operations at our MSM subsidiary. We intend to sell MSM as a going-concern and are in continuing discussions with potential buyers. We expect to complete a sale or other disposition of the MSM operations by the end of 2006; however, we cannot assure you that we will complete a transaction under the terms currently contemplated, or even at all. Similarly, we may incur unanticipated additional costs in connection with the sale or disposition of MSM. If we are not able to sell or dispose of MSM on the terms currently contemplated, our business, prospects, financial condition or operating results could be harmed.

In recent years, we have sold or wound down the operations of other businesses as well.

For more information on these discontinued operations, please see our current Form 10-K, *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations - Discontinued Operations* and Note 16 to our consolidated financial statements. Our consolidated financial statements reflect, under the heading Discontinued Operations, our estimate of the net losses we expected from these operations through the date we estimated they would be disposed, and all losses expected to be realized upon the disposal of these operations. Even after the disposition of these businesses, we may continue to be exposed to some liabilities arising from their prior operations. Additionally, when we sell one of our subsidiaries, the operative contractual agreement may contain provisions that require us to indemnify the purchaser for certain liabilities that arose prior to the sale date but that are discovered afterwards. Even though these liabilities are often capped, until the indemnification period expires, we may continue to be exposed to such liabilities.

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Item 6. Exhibits

Exhibits required by Item 601 of Regulation S-K:

The following lists certain exhibits either filed herewith or filed with the SEC during the fiscal quarter ended September 30, 2006.

Exhibit No.	Description
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
32	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended.

Filed herewith

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

MANTECH INTERNATIONAL CORPORATION

Date: November 6, 2006

By: /s/ GEORGE J. PEDERSEN

Name: **George J. Pedersen**

Title: **Chairman of the Board of Directors and Chief Executive Officer**

Date: November 6, 2006

By: /s/ KEVIN M. PHILLIPS

Name: **Kevin M. Phillips**

Title: **Chief Financial Officer**